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Politics this week

Jan 19th 2006
From The Economist print edition

AFP

Osama bin Laden allegedly warned of fresh terrorist attacks in America in an audiotape broadcast by al-Jazeera, and also announced a surprising truce in Iraq and Afghanistan to assist reconstruction efforts there. If genuine, the tape represented Mr bin Laden's first such address for over a year, following a videotaped message broadcast by al-Jazeera shortly before America's 2004 presidential election. Validation of the tape would scotch popular speculation that the al-Qaeda leader is incapacitated or dead.

Having declared their negotiations with **Iran** at an end, after its decision to resume uranium-enrichment work at its plant at Natanz, Britain, France and Germany huddled with America, Russia and China and then called for an emergency meeting of the board of the International Atomic Energy Agency, the UN's nuclear watchdog. When it meets, starting on February 2nd, the Europeans hope to win agreement for a speedy referral of the matter to the UN Security Council. Meanwhile in both Israel and America there were calls for the use of force not to be ruled out, if Iran continues to be defiant. See article

Laurent Gbagbo, the president of **Côte D'Ivoire**, urged his supporters to end a series of violent protests and attacks on UN peacekeepers. Mr Gbagbo's supporters were angered by what they consider to be foreign meddling in the war-torn West African state, after a UN group recommended that parliament should be dissolved.

The presiding judge in the trial of **Saddam Hussein** and seven of his colleagues, who are accused of killing more than 140 people in a Shia Arab village in 1982, threw the case into disarray by resigning, complaining of political and media pressure. The case is due to resume on January 24th, with one of the four other co-judges taking the court's top spot.

The emir of **Kuwait**, Sheikh Jaber al-Sabah, died aged 78, after 28 years in office. He fled to Saudi Arabia, where he died, when his state was invaded in 1990 by Iraq under Saddam Hussein. See article

Rebels from a previously unheard-of group in **Nigeria's** oil-rich Niger Delta region blew up an export terminal, kidnapped four foreign oilmen in an offshore field belonging to Shell, killed four soldiers nearby, demanded that all exports cease, and told Shell to pay $1.5 billion to one of the delta's states. See article

Ellen Johnson-Sirleaf was installed as **Liberia's** president. She is Africa's first elected female head of state.

Small mercies

In a blow to the Bush administration, the **Supreme Court** upheld Oregon's assisted-suicide law. Other states may push ahead with laws to allow doctors to prescribe drugs to help terminally ill people end their lives. Separately, the court avoided giving a major ruling on abortion, sending a case about New Hampshire's parental notification law back to a lower court. See article

Trent Lott announced that he would after all seek a fourth term as a senator for Mississippi. The former Republican majority leader hinted he might pursue another leadership position in Congress.

Civil liberties groups filed lawsuits in Detroit and New York to stop the government's controversial **domestic eavesdropping programme**.

Chile's first lady

AP

Michelle Bachelet was elected as **Chile's** new president, defeating a conservative opponent and giving a fourth consecutive term to the centre-left Concertación coalition. She is the first woman to be elected president of Chile, only the third woman to be elected president of a Latin American country, and the first who is not the widow of a prominent man. See article

Evo Morales, **Bolivia's** president-elect, wrapped up an eight-country world tour in Brazil, where he said he would not expropriate the investments in natural gas by Petrobras, the state-owned energy firm. Bolivia's outgoing caretaker president sacked the head of the army, after he admitted that he had yielded to American pressure to destroy 30 ageing surface-to-air-missiles ahead of the election. See article

Polls suggested that **Canada's** federal election on January 23rd would see the Conservatives return to power for the first time since 1993, though it was not clear whether they would win an overall majority in the House of Commons. See article

Torture and mistreatment had been a deliberate part of the Bush administration's war against terrorism, undermining the global defence of human rights. So said the annual report of Human Rights Watch, a lobby group based in New York.

Angela's lashes

The leaders of **Germany and Russia** met in Moscow. The atmosphere was frostier than when Gerhard Schröder was German chancellor, since his successor, Angela Merkel, made critical comments about Chechnya and about Russia's clampdown on non-governmental organisations. See article

Russia was gripped by a spell of intense cold, with temperatures in Moscow falling to their lowest in 50 years. Some European customers said that gas supplies from Russia had dipped as Russian consumers needed more for heating.

Moldova's dispute with Russia over gas prices, which had led the Russians to cut off gas supplies for two weeks, was temporarily settled when the Moldovans agreed to increase the price they were paying. The deal will last for only a few months, however.

Lech Kaczynski, the president of **Poland**, gave warning that, unless the centre-right Civic Platform, now in opposition, either joined or backed the right-wing Law and Justice party, he would call new elections in March or April. The previous elections were held only four months ago.

Fighting flu

Donor countries met in China and pledged $1.9 billion—much more than had been expected—for the global fight against **bird flu**.

EPA

Intelligence officials in Pakistan and the United States claimed that an American missile strike in a remote border village in **Pakistan**, which killed some 18 civilians, also killed a number of senior al-Qaeda terrorists, including a master bomb-maker with a $5m bounty on his head. Another of the dead was said to be a son-in-law of Ayman al-Zawahiri, the second-in-command of al-Qaeda.

China and North Korea confirmed that the Korean dictator, Kim Jong Il, had made an “unofficial” visit to China, meeting President Hu Jintao, but this time with no television coverage. China has been trying to persuade North Korea to abandon its nuclear-weapons programme.

In **Taiwan**, both the prime minister and the chairman of the ruling Democratic People's Party were replaced after a defeat for the government in the local elections that took place in December. See article

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Business this week

Jan 19th 2006
From The Economist print edition

The bidding war for **Guidant**, a medical-device company, swung in favour of **Boston Scientific**, which raised its offer to $27 billion with partial backing from Abbott Laboratories. The new bid was about $3 billion higher than one from Johnson & Johnson, a big rival that has five business days to respond to the January 17th offer. Analysts cautioned that Boston Scientific's bid might prove too rich for the smaller company.

Airbus and **Boeing** both set annual records for new aircraft orders in 2005, with the European consortium moving ahead of its American competitor late in the year, thanks to a surge of sales in December. Demand from India was especially strong. China and the Middle East also placed many new orders, but demand from America remained weak. Airbus has beaten Boeing in orders since 2001 and in deliveries since 2003.

Technical hitch

Intel and **Yahoo!** reported disappointing results, raising concerns about slowing technology spending. Intel's fourth-quarter revenue of $10.2 billion was below expectations, a result attributed partly to poor sales of desktop processors. Yahoo!'s fourth-quarter adjusted net income rose 32% from a year earlier, but analysts see the company falling behind Google in profiting from the boom in online advertising. **Apple's** revenue and profits hit all-time highs, and **eBay** also had strong results but shares of both fell nonetheless. **IBM** said its quarterly profit rose by 13%, beating many expectations.

Livedoor, once a high-flying Japanese internet company, was raided by investigators from Tokyo's district prosecutor's office. The firm, which has been known for bold tactics including launching a hostile bid for a subsidiary of a big television broadcaster, is being investigated for allegedly misleading investors with false information. Takafumi Horie, livedoor's founder, has pledged to co-operate. Nonetheless, the company's share price tumbled. See article

The **Tokyo Stock Exchange** had an active week. The Nikkei plunged for two days after the raid on Takafumi Horie's livedoor internet group. Trading was suspended 20 minutes before the close on January 18th lest its computer system fail, another embarrassment for the exchange, which also delayed plans for an initial public offering. See article

More for less

The **productivity-growth rate** in America slowed to 1.8% in 2005, down from 3% in 2004, according to the Conference Board. This was well ahead of growth in the 15 “old” European Union states, which was a mere 0.5%, and nearly equivalent to that of Japan. Although most developed countries had slower productivity growth last year, many emerging markets, including eastern Europe, India and China, saw it surge.

The private-equity consortium bidding €7.3 billion ($8.8 billion) for **VNU** has lined up five global investment banks to back its offer. The bidders include Blackstone Group, Carlyle Group, Kohlberg Kravis Roberts, Thomas H. Lee Partners, AlpInvest Partners, Permira and Hellman & Friedman. Meanwhile, the Dutch media and information business was hit with a credit downgrade by Standard & Poor's, putting it one notch above junk grade.

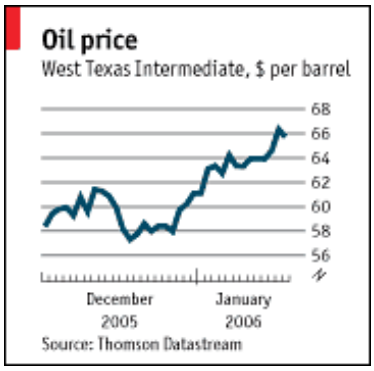
A report by the heads of Europe's largest **financial-services groups** said European consumers are overpaying for banking and insurance services in many countries. A working group on consumer protection blamed governments for blocking the harmonisation of rules in financial services. It called on the European Union to force harmonisation in “essential” areas of consumer protection.

Facing mounting competition from overseas rivals, **Lloyd's of London** launched a three-year plan that includes a review of rules and procedures designed to retain existing insurance business and attract new custom. Some of the best-known syndicates at Lloyd's, including Hiscox, Amlin, Catlin and Wellington, have recently expanded, established or acquired operating units in America and Bermuda.

Gold prices rose above $560 a troy ounce before falling back a bit. Analysts pointed to several possible factors behind the price rise, including Middle Eastern buying, recent rumours that the Chinese central bank may have amassed big reserves, and growing investment in commodity index funds.

In the black again

The **price of oil** rose to nearly $67 per barrel, the highest level in almost four months, before falling back slightly. The price rise reflected threats from Nigerian militants to disrupt the country's oil industry and nervousness about a potential disruption of supply from Iran. See article



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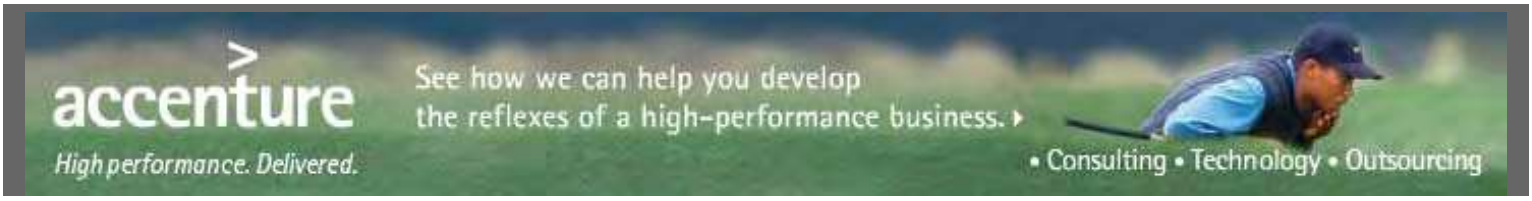
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Economist.com **OPINION**

Old media

King content

Jan 19th 2006
From The Economist print edition

Don't write off Hollywood and the big media groups just yet

"PAIN is temporary, film is forever." That hopeful thought, which found its way into the original script of Peter Jackson's recent re-make of "King Kong", might be seized upon by today's beleaguered entertainment industry. Media companies are suffering intense pain—and it is starting to seem worryingly permanent. In America shares of "old" media firms such as News Corporation, Comcast and other giants of television, film, radio and print, have fallen 25% behind the S&P 500 in the past two years, despite some heroic financial results. Meanwhile, the market value of Google, which made its debut on the stockmarket in 2004, is now equal to the combined worth of Walt Disney, News Corporation and Viacom, three beasts of the old media jungle. One investor, who recently moved two-thirds of his $1 billion fund out of American media and into emerging-market companies, moans that "the market thinks something's going to get them, whether it's piracy, personal video recorders, or Google."

Desperate to rescue its share price, Viacom broke itself in two on January 3rd. Time Warner, the biggest media group of all, is under attack from Carl Icahn, a corporate predator perfectly adapted to sniff out the weak and vulnerable. The big groups have seen their newspapers and magazines lose readers and advertising to the internet; their music businesses suffer piracy and falling sales; and someone else's video games captivate new generations of consumers. Now come fears about film and TV, the bedrock of their business.

Hollywood took 7% less at the box office in 2005 than in 2004 and growth in sales of DVDs has slowed. Internet video threatens the satellite and cable systems of companies such as News Corporation and Time Warner. Dozens of advertisers are shifting budgets from television to such places as the internet and billboards. Brand-owners hate it that people are using digital video recorders to avoid their pitches. And if media firms move on to the internet themselves, they risk losing their films and television programmes to pirates.

Moguls still

No wonder that on media island they are downcast. Yet, if Hollywood teaches one thing, it is that stories can be re-made and dreams can come true. Rather as big retailers, including Wal-Mart and Tesco, have discovered advantages online, so too will big media companies.

True, the internet and digital devices will eventually break those companies' grip on distribution. But they gain something else: a digital world in which what you supply matters far more than how you supply it. In satellite

radio, for example, Sirius has crept up on XM Satellite Radio thanks chiefly to its content, in the controversial form of Howard Stern. And this world holds another promise, too: an abundance of virtually costless ways to supply consumers with what they want to watch, whenever they want it—things established media are ideally placed to provide.

The internet is still in the digital equivalent of the silent-film era. It has been formidable for text, still images and music, but is only now, with broadband access, entering an age of high-quality video. As it does so, Time Warner, News Corporation, Disney and other media companies will be able to cash in on their film and television archives. Selling video direct to consumers, without distribution getting in the way, lets media firms, and viewers, mine their vaults for old episodes of “The Outer Limits”, Johnny Carson, or whatever: minority tastes, to be sure, but taken together, a vast new market.

Moreover, old media will command audiences for many years yet. New media understand this: Google has just bought dMarc, which sells old-fashioned radio advertising. Websites, such as BabyCenter.com and AlwaysOn, have recently launched print-magazine versions of themselves, to capture advertising that was out of their reach online. As the best remaining source of a mass audience, TV and film are the best places to create and promote the next “Simpsons” or “Narnia”.

Some people worry that new media companies may over time shunt old ones aside as producers of content. Certainly, digital media will create new stars and new businesses, but making high-quality video content will always be a daunting and expensive task. Music or a blog can be composed from a bedroom, but not an episode of “Friends”. Just last month DreamWorks, Hollywood's youngest studio, sold itself to Viacom, despite its strong financial backing and the talent of Hollywood luminaries. It made some money, but could not afford a billion-dollar investment in films year-in, year-out. Yahoo! has a media unit, but so far it hasn't had any hits. Responding to the news this week that Yahoo! intends to spend up to $10m on a reality-TV concept called “The Runner”, analysts complained that the investment would damage its margins.

By contrast with Yahoo!'s dabbling, old media is now investing in digital media in earnest. It all went terribly wrong before 2000 when bewitched executives squandered money on the internet and Time Warner sold itself to AOL in one of history's worst-ever deals. But now they are back. Rupert Murdoch, chief executive of News Corporation, made a series of acquisitions in 2005 (see article). Disney is supplying two hits, “Desperate Housewives” and “Lost”, using Apple's iTunes download service. Last summer Viacom bought Neopets.com, a virtual-pets site. Old media is well placed to steer its huge offline audiences to its websites.

Helpfully on cue, piracy now seems less of a threat. The music industry now has a healthy business in legal downloads. Operators of peer-to-peer networks, such as eDonkey, are going straight. And Hollywood is realising that it has no equivalent to a big musical weakness—that many albums consist of a few decent tracks padded by dross.

Any media business has two products to sell: its content (to readers and viewers); and its audience (to advertisers). The task for old media is first to protect its advertising revenues by amassing audiences online and, second, to offset their viewers' intolerance of mass-advertising by making them pay more for content—which they are increasingly willing to do. It will not be easy, but then saving the heroine never was.

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Economist.com OPINION

South America

Bolivia takes on the superpower

Jan 19th 2006
From The Economist print edition

The United States can afford to relax

Reuters

WHATEVER else you may think about Evo Morales, the leader of Bolivia's coca-farmers who will become his country's president on January 22nd, he cannot be accused of underestimating his own importance in the scheme of things. The man about to inherit the problems of a chaotic, dirt-poor country of fewer than 9m people in the Andes boasts that he is the “worst nightmare” of the United States (see article). The boast, of course, is preposterous. The worry is not what he might do to the United States but what the United States, also exaggerating his significance, might do to him.

For two years Mr Morales has done his best to upset South America's established order. The protests he has led have toppled two presidents in Bolivia. He has campaigned to nationalise its rich deposits of natural gas and to stop the eradication of coca, the stuff from which cocaine is manufactured. He seems intent on cocking a snook at the superpower. Mr Morales is just back from a world tour, in an aircraft provided by his friend, Hugo Chávez, Venezuela's self-styled “21st century socialist” president. His first visit was to Fidel Castro in Cuba. Then, in Caracas, Mr Chávez invited Mr Morales into a *Yanqui*-bashing “axis of good” with Cuba and Venezuela. In Beijing Mr Morales pronounced himself an “ideological ally” of China. It is easy to see why the Americans might wish to undermine him rather than watch Bolivia turn into a cross between a Chávez-style elected autocracy and a narco-state.

But that would be a grave mistake. America has few, if any, vital interests in Bolivia. The main gas companies there are European and Brazilian, not American. Mr Morales's opposition to coca eradication will worry the drug warriors in Washington: it comes just when a squeeze on coca production in Colombia is at last having an impact on the street price of cocaine in the United States. But most Bolivian cocaine goes to Brazil and Europe—and “victories” over drugs tend anyway to be temporary blips in an unwinnable war.

The real interest of the United States in Latin America lies in supporting democracy. That means doing its best to work with Mr Morales, who with 54% of the vote in December's election has the strongest mandate of any Bolivian president since 1960. Although his election has been seen as part of a broader swing to the left in Latin America, the region in fact has two sharply differing lefts. One is made up of radical anti-American populists, epitomised by Mr Chávez. The other is social-democratic and economically responsible. This one includes Brazil's Luiz Inácio Lula da Silva and Michelle Bachelet, elected on January 15th as Chile's new president (see article). Despite appearances, there are some grounds to hope that Mr Morales can be wooed to the second camp.

Behind the rhetoric, the new president shows an appreciation of the realities of power. He chose, for example, to

fly from Havana to Caracas via his own capital, for a meeting with the American ambassador. America is, after all, Bolivia's biggest aid donor. In both Spain and Brazil, Mr Morales spoke soothingly of negotiating with the gas companies, rather than of expropriation. Behind his victory lies a hunger for economic progress. To deliver that he will have to use Bolivia's gas to alleviate poverty, and improve infrastructure and education while not scaring away the private investment the country needs. It is possible that impatience and his more radical supporters will push him into Mr Chávez's camp. But he is duly elected. And for now he deserves the benefit of the doubt.

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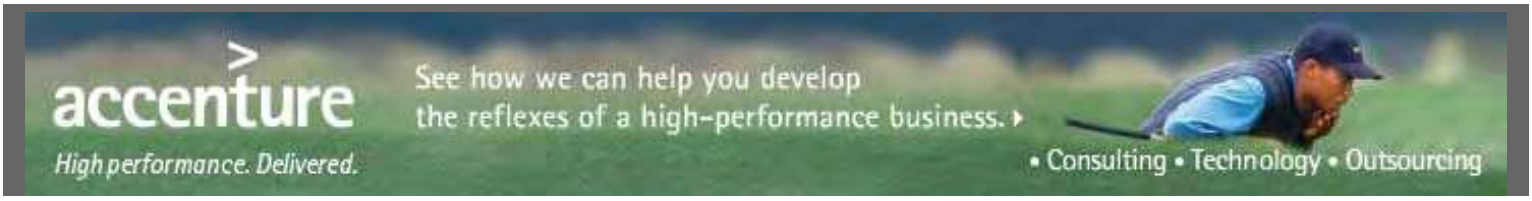
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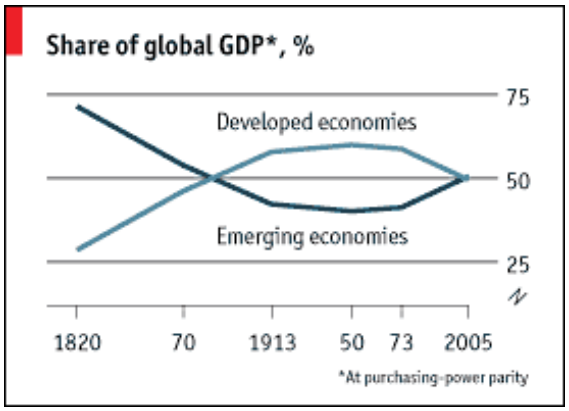
Economist.com **OPINION**

Emerging economies

Coming of age

Jan 19th 2006
From The Economist print edition

The rich nations no longer dominate global production



THREE striking facts highlight the dramatic shift in recent years in the relative economic balance of “first-world” and “third-world” economies. Last year, according to our estimates, emerging economies produced slightly more than half of world output measured at purchasing-power parity. Second, they also accounted for more than half of the increase in global GDP in current-dollar terms. And third, perhaps most striking of all, the 32 biggest emerging economies, which we track weekly in *The Economist* and *Economist.com*, grew in both 2004 and 2005. Every previous year during the past three decades saw at least one country in recession—if not a deep crisis. Some economies will inevitably stumble over the coming years, but, thanks to sounder policies, most can look forward to rapid long-term growth (see article). The young emerging economies have grown up in more ways than one.

Such happenings are part of the biggest shift in economic strength since the emergence of the United States more than a century ago. As developing countries and the former Soviet block have embraced market-friendly economic reforms and opened their borders to trade and investment, more countries are industrialising than ever before—and more quickly. During their industrial revolutions America and Britain took 50 years to double their real incomes per head; today China is achieving that in a single decade. In an open world, it is much easier to catch up by adopting advanced countries' technology than it is to be an economic leader that has to invent new technologies in order to keep growing. The shift in economic power towards emerging economies is therefore likely to continue. This is returning the world to the sort of state that endured throughout most of its history. People forget that, until the late 19th century, China and India were the world's two biggest economies and today's “emerging economies” accounted for the bulk of world production.

Fear or cheer?

Many bosses, workers and politicians in the rich world fear that the success of these newcomers will be at their own expense. But rich countries will gain more than they lose from the enrichment of others. Fears that the third world will steal rich-world output and jobs are based on the old fallacy that an increase in one country's output must be at the expense of another's. But more exports give developing countries more money to spend on imports—mainly from developed economies. Faster growth in poor countries is therefore more likely to increase the output of their richer counterparts than to reduce it. The emerging economies are helping to lift world GDP growth at the very time when the rich world's ageing populations would otherwise cause growth to slow.

Although stronger growth in emerging economies will make developed countries as a whole better off, not

everybody will be a winner. Globalisation is causing the biggest shift in relative prices (of labour, capital, commodities and goods) for a century, and this in turn is causing a significant redistribution of income. Low-skilled workers in developed economies are losing out relative to skilled workers. And owners of capital are grabbing a bigger slice of the cake relative to workers as a whole.

As a result of China, India and the former Soviet Union embracing market capitalism, the global labour force has doubled in size. To the extent that this has made labour more abundant, and capital relatively scarcer, it has put downward pressure on wages relative to the return on capital. Throughout the rich world, profits have surged to record levels as a share of national income, while the workers' slice has fallen. Hence western workers as a whole do not appear to have shared fully in the fruits of globalisation; many low-skilled ones may even be worse off. But this is only part of the story. Workers' wages may be squeezed, but as consumers they benefit from lower prices. And as shareholders and future pensioners, they stand to gain from a more efficient use of global capital. Competition from emerging economies should also help to spur rich-world productivity growth and thus average incomes.

To the extent that rich economies as a whole gain from the new wealth of emerging ones, governments have more scope to compensate losers. Governments have another vital role to play, too. The intensifying competition from emerging economies makes flexible labour and product markets even more imperative, so as to speed up the shift from old industries to new ones. That is why Europe and Japan cannot afford to drag their heels over reform or leave workers ill-equipped to take up tomorrow's jobs. Developed countries that are quick to abandon declining industries and move upmarket into new industries and services will fare best as the emerging economies come of age. Those that resist change can look forward to years of relative decline. Those that embrace it can best share in the emerging economies' astonishing new wealth.

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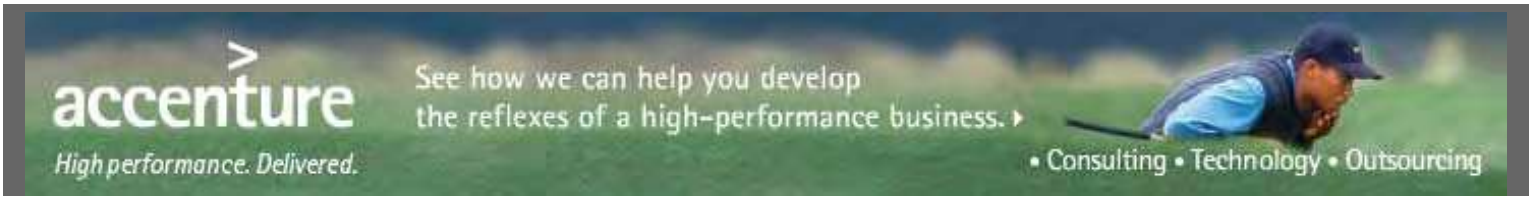
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Economist.com **OPINION**

Canada

Those daring Canadians

Jan 19th 2006
From The Economist print edition

And why they should vote Conservative this time

Reuters

AS THEY made clear when America had one in the 18th century, Canadians do not much like revolutions. But if the pollsters are right, something that will pass north of the 49th parallel for a revolution is indeed about to occur. In the general election due on January 23rd (see article), Canadian voters seem set to sack their Liberal government and put the Conservatives back into power for the first time in 12 years.

On the face of it, the sacking seems perverse, and ungrateful. The Liberals have given Canada a long period of stable politics, enlightened social policy and economic growth, boosted lately by the world's growing appetite for Canada's plentiful energy and natural resources. Although the prime minister, Paul Martin, has had the top job only since the end of 2003, he gave a stellar performance as finance minister in the years before that, restoring order to public finances the Tories had left in chaos. By comparison, his Conservative challenger, Stephen Harper, is an unknown quantity, untested by previous high office and until recently written off as a not especially competent leader of the opposition. In short, barring a last-minute reversion to type as they enter the polling stations, Canadians seem to have decided to take a gamble. Gambling will be out of character. It will also, on this occasion, be right.

The Liberals have done many good things over the past 12 years, but have lately succumbed to the three familiar vices of a party that has been too long in power. The first of these is sleaze. Mr Martin would not be holding this unpopular mid-winter election at all but for the unearthing of a decade-old financing scandal under which public money intended to promote the federal cause in Quebec was diverted to the Liberals and their cronies. The second is fractiousness. Mr Martin became prime minister only after mounting a palace coup against his predecessor, Jean Chrétien. Instead of uniting around the new leader, the party thereupon coalesced around two sullen and unforgiving camps. The last is directionlessness. However stellar his performance as a finance minister, Mr Martin has failed as prime minister to convey a sense of policy priorities to his demoralised civil servants or of national purpose to Canadians at large.

The west's turn

The vices of prolonged incumbency might be enough to persuade voters in almost any democracy that it was time for a change. But Canada has another reason on top of this to welcome a Conservative victory. Over recent years,

many people in western Canada, where the Conservatives are strongest, have come to believe that their part of the country does not get a fair hearing in Ottawa, where national politics is traditionally dominated by Ontario and Quebec, and the latter's constant talk of secession. Westerners ruefully note that since 1968 Canada has spent 36 years under prime ministers who come from Quebec, or represent constituencies in Quebec, and a mere 15 months under prime ministers from the west. As an adopted westerner, Mr Harper might therefore be in a good position to inject new unity into a federation under strain.

Much depends, of course, on what Mr Harper and his party actually do with victory if they win. The Liberals portray the Conservatives as sinister social extremists, intent on importing dangerous neo-conservative ideas from the United States. In the election of June 2004, this line played well, not least because of the extreme unpopularity of George Bush in Canada. Half way through the campaign, voters switched away from Mr Harper for fear that he would turn too sharply right on economic, social and perhaps even foreign policy.

This time, Mr Harper has been cannier, moving to the centre where Canadians feel comfortable. Though the Conservatives say they will cut some taxes, the Liberals have proposed tax cuts too. And Mr Harper has made it plain that he will do nothing too radical to Canada's generous welfare model or cherished public health service. If he is to be believed, a somewhat left of centre government will be superseded by a somewhat right of centre government. Contrary to what the Liberals say, this will not turn Canada into the United States. Indeed, by America's standards, Canada's gamble may turn out to be a pallid affair. All the more reason to risk a flutter.

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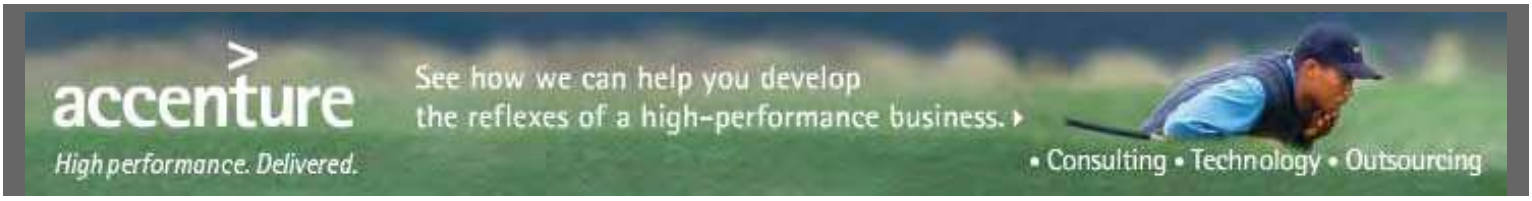
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Economist.com **OPINION**

Nutrition

Food for thought

Jan 19th 2006
From The Economist print edition

In praise of omega-3s

SPL

DRINKING fruit juice may once have cost British sailors the indignity of being called “limeys”, but it also saved them from scurvy, just as liver helps to treat night blindness and unpolished rice prevents beriberi. These once-mysterious properties have a simple explanation. The body is remarkable at using dazzlingly complex combinations of a few abundant molecules from food to accomplish most of what it needs. But it cannot bodge everything, so it must also have a small amount of other nutrients. The list includes several vitamins and inorganic minerals as common as salt and as rare as selenium or iodine. And it has just got longer, with the addition of omega-3 fatty acids, found in fish, which have made the transition from health-food fad to vital nutrient with amazing speed.

To combat the threat to public health from a lack of these nutrients, governments encourage food makers to add them to some products. So iodine, which prevents goitre, is routinely added to salt and vitamins to breakfast cereals. They also issue figures for recommended daily allowances of these nutrients that duly appear next to the ingredient lists on food packets—and are duly ignored.

Some people see this, and the accompanying campaigns to persuade people to eat healthy food, as a nannying intrusion into personal freedom. That is a moot point when the taxpayer so often has to pick up the bill for the medical consequences of careless eating. But there is one area in which the state is generally felt, even by most libertarians, to have a legitimate interest, and that is the protection of children. Children cannot necessarily make informed decisions and neither can their parents on their behalf, be they ever-so loving. And that concern is particularly relevant when a child is not yet born.

Science has shown that many adult diseases, from obesity and diabetes to high blood pressure (which leads to heart disease and kidney failure) have their origins in how the fetus is fed. Indeed, this particular cluster of symptoms is seen by a growing number of workers in the field as a single disease, known variously as metabolic syndrome or syndrome X.

The latest piece of research is into omega-3 fatty acids. Their effects on adults are well established (they can, for example, reduce the feeling of anger in some people who cannot control their tempers). But it now seems that an inadequate intake of them by a pregnant woman puts her child at greater risk of being stupid, clumsy and friendless.

That, at least, is the conclusion of an Anglo-American study whose results have just been made public (see article). The researchers showed that the children of mothers who ate food with little omega-3 content had a lower IQ than their peers, found normal social relations harder to deal with, and lacked fine-tuned physical co-ordination.

Cui bono?

This kind of research ought to be of interest to all governments trying to address educational problems and anti-social activities. Intervening in fetal nutrition is not a simple matter, of course. For instance, the researchers note that American guidelines recommending that pregnant women should not eat fish because it may contain mercury have the perverse effect of cutting off those women (and their fetuses) from one of the best sources of omega-3s. However, although science is continually shifting, it is not arbitrary. You can, for instance, depend on sunlight to stave off rickets today just as you could when its benefits were discovered 90 years ago.

So, although nobody would suggest that fixing maternal nutrition now would cure bad behaviour in 20 years' time and result in a nation of geniuses, there is an increasing amount of evidence that it would help. Some American school districts now recognise the part nutrition plays in learning—and offer breakfast to pupils who have not eaten at home.

Dealing with maternal malnutrition (which is not the same as undernutrition) is even more important, because environmental damage wrought in the womb is as irreversible as the effects of bad genes. It is surely cheaper to make interventions that have an impact early on than to react later. The modern version of the age-old wisdom still applies: 28.3g of prevention is worth 0.454 kilos of cure.

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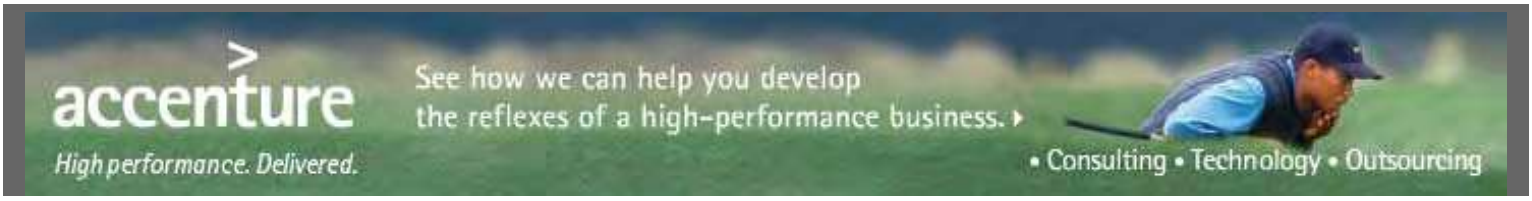
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OPINION
LETTERS

On Devan Nair, American poverty, the death penalty, evolution, Deutsche Bank, gay marriage

Jan 19th 2006
From The Economist print edition

The Economist, 25 St James's Street, London SW1A 1HG
FAX: 020 7839 2968 E-MAIL: letters@economist.com

Devan Nair

SIR – In your obituary you wrote "by Mr Nair's account, Mr Lee promised to crush him [J.B. Jeyaretnam], crying 'I will make him crawl on his bended knees and beg for mercy.' That image had haunted Mr Nair before, as the worst expression of arrogant colonialism" ("Devan Nair", December 24th).

This and many other statements Mr Nair made after his bout of alcoholism in 1985 were unfounded. One statement he made in 1991 forced Mr Lee Kuan Yew to sue him and the Canadian *Globe & Mail* in Toronto. The matter was settled when Mr Nair's two sons issued this statement, reported in the *Globe & Mail* on July 1st 2004:

"Mr C.V. Devan Nair, aged 80, has been diagnosed as suffering from the beginning stages of dementia, an ailment which affects his memory. He is no longer able to give evidence in court proceedings.

"On March 29th 1999, the *Globe & Mail* published an article by Mr Marcus Gee. The article quoted Mr Nair as saying that Mr Lee Kuan Yew had Singapore government doctors slip hallucination drugs to Mr Nair to make him appear befuddled.

"Having reviewed the records, and on the basis of the family's knowledge of the circumstances leading to Mr Nair's resignation as president of Singapore in March 1985, we can declare that there is no basis for this allegation."

Yeong Yoon Ying
Press secretary to Minister Mentor
Singapore

Apology: We recognise that the statements attributed to Mr Lee in the obituary on Devan Nair and which are referred to in Mdm Yeong Yoon Ying's letter above, are false. We apologise to Mr Lee for having published them, and we unreservedly withdraw them. We have agreed to pay Mr Lee damages and to indemnify him for all costs incurred by him in connection with this matter.

Comparative poverty

SIR – Regarding your comparison of poor people in the United States with poverty in Congo ("The mountain man and the surgeon", December 24th). I have met many middle-class Asians from poor countries who are certainly better off than the man from eastern Kentucky that you profiled, so I find your choice of Congo to illustrate life in the developing world an extreme one. Unlike China, India and South-East Asia, where over half the world's poor live, Congo is in chaos and is emerging from one of the world's bloodiest conflicts.

Karl Benson
Boston

SIR – When explaining why American poverty statistics are misleading you forgot one crucial component of their unreliability: poverty thresholds are measured at the national level and do not differ between regions based on the

cost of living. While conducting research on Head Start children's programmes, this minor detail caused me the utmost frustration, as the “estimate of how much an adequate diet might cost” is assumed to be the same everywhere. The cost of living may well be less in Kinshasa than it is in eastern Kentucky, but I can assure you it is less in eastern Kentucky than it is in New York.

Joanna Hootnick
New York

SIR – To conclude that “if poor Americans were to compare their standard of living with what is normal elsewhere in the world, let alone in Congo, they would see that they have little cause for discontent” is rock bottom in terms of intellectual hollowness.

Wolfgang Mostert
Gentofte, Denmark

Death penalty

SIR – I take issue with your stance against the refusal to pardon Stanley “Tookie” Williams, who started the Crips gang (“After Tookie”, December 17th). Although I am opposed to the death penalty in principle, granting selective clemency to criminals on death row is illogical. Abolition requires a political and moral sea change, not arbitration on a case-by-case basis. If anything, pardoning such a controversial figure could further galvanise the majority, who still support state executions. Moreover, as a resident of South Central I can tell you that the Crips gang continues to be a destructive influence, despite Mr Williams's rehabilitation. No matter how many books Tookie wrote, his hands were still bloodied by multiple murders and his crimes cannot be undone.

Eugene Marder
Los Angeles

SIR – Politicians should not be burdened with final authority over the death penalty. Such a serious matter is the province of the legal system and only the legal system. The whole procedure needs reviewing.

William Kelly
Frinton-on-Sea, Essex

Evolving faith

SIR – I am amazed at your faith in evolution (“The story of man”, December 24th). It far outweighs my faith in creation. My faith requires only one mechanism: God's love. Yours requires three: that something can come of nothing (the “Big Bang”), that rocks can spontaneously spawn living things (life from inorganic elements) and that genetic mutations can turn a flatworm into an Einstein. You win; there is no doubt that your faith far outweighs mine.

Stephen Brahm
California

SIR – To state that there were three secular faiths, Darwinism, Marxism and Freudianism, in the 19th century is not completely correct. Marxism was obviously a religion and Freudianism must be taken on faith as its theories were based on bad—or no—data. Darwinism, however, is the theory of evolution, with a number of variants, that is based on much peer-reviewed scientific evidence. That is not faith.

Gary Bennett
Idaho

SIR – Darwinist evolution may help explain the open-endedness of economic growth, but it is scant justice to use this argument to de-throne Adam Smith as the founding father of economics (“The proper study of mankind”, December 24th). Even before Darwin, Adam Smith wrote that a person's desired level of income should be such that it allow them to live as a respected member of his or her social group—open-ended indeed.

Frans Baneke
Bussum, The Netherlands

Bad business

SIR – I was outraged by your assertion that Josef Ackermann, the head of Deutsche Bank, “should not stand trial” lest “German business may suffer” (Contents, January 7th). The charges in the Mannesmann affair are serious, and the desire to avoid bad publicity is irrelevant to the legal proceedings. Fortunately your more balanced leader on Mr Ackermann did not state the same position (“The trials of Josef A”, January 7th).

Mitja Müller
Bremen, Germany

Happy union

SIR – I take issue with the religious right wanting to ban gay marriage and I believe that we should all be in favour of same-sex nuptials (“Bah, humbug”, December 24th). After all, why should gays be exempt from misery?

Michael Spivey
Hong Kong

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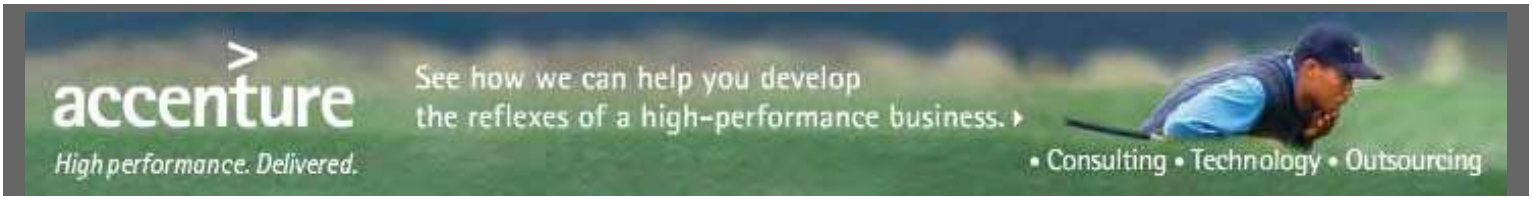
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OPINION
LETTERS

Apology: Mr Lee Kuan Yew

Jan 19th 2006
From The Economist print edition

The Economist, 25 St James's Street, London SW1A 1HG
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We recognise that the statements attributed to Mr Lee in the obituary on Devan Nair and which are referred to in Mdm Yeong Yoon Ying's letter, are false. We apologise to Mr Lee for having published them, and we unreservedly withdraw them. We have agreed to pay Mr Lee damages and to indemnify him for all costs incurred by him in connection with this matter.

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Economist.com WORLD

Bloodless regime change

A rainbow of revolutions

Jan 19th 2006
From The Economist print edition

If outsiders make such a mess of getting rid of despots, why not encourage the locals to have a go?

Reuters

THE Iranian government is annoying. Despite its denials, it seems determined to make a nuclear bomb. It is neither persuaded by diplomacy, nor cowed by the threat of sanctions, nor worried by the possibility of attack. And in truth outsiders are pretty powerless. But don't worry: their easiest option—to wait—may not be such a bad one. With luck, it is only a matter of time before decent, sensible Iranians rise up and overthrow the religious zealots and incompetent populists who rule them. As frequent protests show, discontent is widespread: women publicly campaigned for their rights during the presidential campaign last June, Tehran's bus drivers struck last month. The old are fed up, and feel betrayed. The young want jobs and fun. In fact, Iran is ready for revolution. Surely it will be the next country to see a magnificently non-violent, colour-coded, do-it-yourself regime change?

It is certainly a beguiling thought. Iraq has proved a sobering experience for those who thought a small war was all that was needed to replace an unpopular tyranny cheaply and painlessly with a friendly democracy. The removal of Saddam Hussein has certainly not been the exemplary exercise that would, some Americans believed, serve as a model across the ripe-for-reform Middle East. Meanwhile, however, the world has marvelled at the way one stinker after another has been almost elegantly thrown out of office—most recently in Georgia, Ukraine and Kirgizstan—with scarcely any trouble or expense on the part of outsiders. How nice if the Iranians would now oblige, too.

People power has actually been around for a while. The 20th century was so horribly bloody that it has been easy to overlook the potency of peaceful boycotts, strikes, civil disobedience and public protests in many of the greatest upheavals of the past hundred years. In their book, “A Force More Powerful”, Peter Ackerman and Jack Duvall chronicle some of those events: the popular uprising in Russia in 1905, Mohandas Gandhi's campaign for Indian independence, the Danes' resistance to the Nazis, Martin Luther King's civil-rights campaign in America, Solidarity's triumph in Poland, the noisy clattering of pots and pans in Chile in 1983 that sounded the beginning of the end for Augusto Pinochet, the demonstrations that eventually drove Ferdinand Marcos of the Philippines from office in 1986, the first Palestinian *intifada*, the Tiananmen protests in 1989, and others. Few of these brought about an instant change of regime, but all of them proved seminal: that is, they planted the seeds of change.

The secret of people power's success is simple: a tyranny can cut off one head or even 1,000, but 10,000 or 100,000 is much more difficult—and becoming more so with time. Stalin and Mao got away with it, because

nobody dared risk a world war by taking them on, and Pol Pot and the Rwandan *génocidaires* got away with it because nobody cared enough to stop them. But the last Soviet dinosaurs shied away from it, and even Erich Honecker's East German thugs decided not to use force to stop the mass migration of their citizens through Hungary to the West, thus ensuring the collapse of European communism. In East Germany, small civil-rights, environmentalist and women's groups that had quietly been incubating in the Lutheran church suddenly and confidently emerged. Then came mass rallies in East Berlin, Dresden, Leipzig and other cities, from which arose the cry, “We are the people!” It was all too much, even for an apparently ruthless and monolithic system of control.

That communism could be thus brought down, gloriously and bloodlessly, sent shivers of fear through the world's despots, and of exhilaration through their subjects. The implacable white South Africans who sustained fortress apartheid now realised that they could not hold out indefinitely: more than ever, the use of force, their traditional response to peaceful boycotts, rent strikes, demonstrations and the country's range of civil movements, made them look desperate, and robbed them of any claim to be respectable, still less democratic. By February 1990, Nelson Mandela was out of prison, and by 1994 the rascals had been thrown out in a democratic election. People power had not alone been responsible for changing the regime, nor had it all been done non-violently: the main movement, the African National Congress, had a guerrilla army. But non-violent action had surely played a large part in ending apartheid.

Though the ground was rocky and the plant has proved weak, democratisation moved through Africa in the 1990s like feathergrass. Such countries as Benin, Cape Verde, Ethiopia, the Gambia, Ghana, Madagascar, Malawi, Mali, Mozambique, Senegal, Tanzania, Uganda and Zambia all got rid of dictators, moved to a multi-party system or cleaned up their act in other pro-democracy ways, and several were moved to do so only after strikes, demonstrations and other, usually peaceful protests. Something similar happened in countries as far afield as Bangladesh, Guatemala, Indonesia, Mexico, Nepal, Nicaragua, Peru, South Korea and Taiwan.

In Europe, once the most closely controlled satellites of the Soviet Union had been set on a democratic course, Yugoslavia was the next place to be weaned off authoritarianism, and Slobodan Milosevic the next big casualty of popular action. The great demagogue of the Balkans, who had risen to power by putting the fear of St Vitus into the Serb masses, was in October 2000 brought down by the same masses as they turned against him. After 13 years in which he had impoverished his people and led them to defeat in two wars, he tried to ignore the election victory of his opponent. That brought half a million or more Serbs on to the streets of Belgrade, and quite a lot of them storming through the doors of the Yugoslav parliament. Crucially, elements within the police and armed forces changed sides.

The rose revives...

The ripples from that upheaval were soon felt as far away as Côte d'Ivoire, where in 2000 street protesters, openly invoking the example of Yugoslavia, drove General Robert Guei from the presidency that he had seized a year earlier. Bigger tyrannies were soon to totter. Georgia's authoritarian government fell in 2003 in a “rose” revolution brought about, at least in part, by three weeks of protests with tens of thousands on the streets. The next year Ukraine's post-Soviet regime came to a similar dramatic end in an “orange” revolution involving thousands of Ukrainians camped patiently in the December snow.

Then, in March 2005, came the collapse of Lebanon's puppet government after nearly 1m demonstrators had defied a ban on protest against the Syrian masters who pulled its strings. By the end of April, Syria's troops were out and a 29-year military involvement was over. By that time Kirgizstan's unpopular president of 15 years had also been put to flight, after a month of demonstrations that culminated in an exhilarating surge through several government buildings. After that “tulip” revolution, all eyes were on the other Central Asian nasties—in Kazakhstan, Tajikistan, Turkmenistan and especially Uzbekistan, whose president, Islam Karimov, was soon to tell his troops to shoot hundreds of civilians after an uprising that he blamed on Islamist terrorists. But perhaps Iran's rulers should have been just as worried: in Iran, the tulip is the symbol of martyrdom.

Reuters

Boo, a million times boo, to Syria

Don't bank on their early departure. Don't even assume that popular revolutions are always for the good. Some can be bad from the start. In Bolivia, for example, mass uprisings have tended to look rather like mob rule. A country with a long tradition of coups (nearly 200 between 1825 and 1980), it has struggled to adopt the democratic habit, running through five presidents in the past five years (a sixth is sworn in on Sunday). One, Gonzalo Sánchez de Lozada, was driven from office in 2003, just 15 months after his election, by violent clashes over his plan to sell natural gas

to the United States via Chile. “Gas wars”, mostly in the form of protests by indigenous Indians, returned last year, forcing out another president, Carlos Mesa. Bolivia does now have a ruler, Evo Morales, who has been properly elected in a fair election, so the nationalist, left-wing policies of the protesters have won a retrospective endorsement (see article). But that hardly excuses the earlier uprisings.

Many more popular overthrows that at first seemed splendid have turned out badly. To their credit, the Philippines and Indonesia have confounded critics, but optimists have been disappointed in several African countries, and Nepal looks awful. Perhaps the most disillusioned revolutionaries, though, are the orange-clad Ukrainians, who last September saw their former hero, Viktor Yushchenko, sack his government amid feuds, splits and charges of corruption, and last week saw their parliament sack its successor. A poll taken in November by Freedom House, an American lobby group, said 60% of Ukrainians, including 44% of those who supported the 2004 protests, thought the country was heading in the wrong direction.

More worrying for some of those Americans who believe that democracy will serve the United States' interests is the possibility that it will be destabilising, or result in the election of hostile governments. It is clear that elections often return to power the people who previously held it undemocratically. That is how virtually all the Central Asian autocrats managed to hold on to office after the Soviet Union broke up in 1991, and the pattern has been slow to change: the tulip-waving demonstrators who denounced President Askar Akaev in Kirgizstan last March are now ruled by his former comrades.

...the hazards, too

Elections are not necessarily free, of course, and even free elections, on their own, do not constitute a democratic system. “As a rule, 'electocracy' should not be confused with democracy,” rightly avers Richard Haass, head of policy planning in the State Department in 2001-03, in his book “The Opportunity”. But even free elections in a truly democratic system might well, in some places, produce an Islamist government.

Is that a risk worth taking? The dissident Mr Haass counsels caution. “It is neither desirable nor practical to make democracy promotion a foreign-policy doctrine,” he says. Too many “pressing threats” get in the way of beautifying the way other countries govern themselves. And America's record seems to bear him out, especially when the war on terror or western energy supplies enter the picture. Central Asia is close to Afghanistan, so the United States maintains a base in Kirgizstan and had one in Uzbekistan too, until it was thrown out last July. Uzbekistan is also one of the countries to which it has “rendered” terrorist suspects. Similarly, in the interests of energy security, it has supported Ilham Aliev, the incumbent despot in Azerbaijan, welcoming the pipeline that now runs through his country. And the politics of oil might also make it difficult to support people power in Saudi Arabia, just as the politics of the entire Middle East has stopped America pressing the democratic case too hard in Egypt.

Still, George Bush often says, as in his inaugural address last year, that “it is the policy of the United States to seek and support the growth of democratic movements and institutions in every nation and culture, with the ultimate goal of ending tyranny in our world.” And the promotion of democracy is now an official objective of countries like Britain, Canada, Germany and the Netherlands. So can people power become an instrument of foreign policy?

Several organisations believe so. America has groups such as the National Endowment for Democracy, the International Republican Institute, the Middle East Partnership Initiative and the National Democratic Institute, all financed by the government. Britain has the Westminster Foundation, also government-backed, and so on. These are not specifically charged with promoting people power, but they sometimes do, as, for instance, in Kirgizstan. The trouble is that, try as they may to present themselves as neutral agents removed from government—the National Endowment for Democracy often describes its activities as “technical assistance”—they are usually seen as arms of the CIA or its equivalent. Genuinely independent NGOs, which were active in the Georgian upheaval and several others, are often similarly tarred.

Even so, it is tempting to think that outsiders can help. It is clear that a successful popular change of regime—one, that is, that results in a reasonably democratic and enduringly free system—is much more likely to emerge if it has certain characteristics. What is needed, according to an analysis by Freedom House of 67 overthrown dictatorships, is “broad-based, non-violent civic resistance—which employs tactics such as boycotts, mass protests, blockades, strikes and civil disobedience to delegitimate authoritarian rulers and erode their sources of support, including the loyalty of armed defenders.” Such people power can be decisive. And if it is a significant feature of the change of regime, the emergence of a free society is much more likely than in a top-down change of power brought about by elites or others close to power. Moreover, the most important factor in contributing to the emergence of a freer society is the presence of strong and cohesive non-violent civic coalitions.

So, if outsiders can encourage any of these features, they may succeed not just in spreading democracy but in state-building. Accordingly, Freedom House suggests donors should support local NGOs, and offer training in coalition-building and non-violent resistance. It and others advocate efforts to help the local media, with training or money for computers, mobile phones or even a printing press: such assistance proved crucial in Kirgizstan.

The International Centre on Nonviolent Conflict, based in Washington, DC, is perhaps more involved in the promotion of peaceful people power than any other organisation. Financed entirely by its own officers, members and employees, it neither takes money from governments nor works with them. It aims to do good by spreading the word. One method is to distribute videos of a documentary series of “A Force More Powerful”, which shows how non-violent resistance can be used to effect change. The videos, translated into Arabic, Chinese, French, Persian, Russian and Spanish, have gone to over 60 countries, greatly displeasing the authorities in Cuba, Iran and Zimbabwe, among others.

The centre will not help anyone directly to overthrow a government. It does, however, run workshops for activists seeking the peaceful promotion of democracy or human rights. These often draw on the experience of those who have successfully used non-violence: a group of Serbs, for example, now travel the world telling the story of Mr Milosevic's downfall and thus giving confidence to those who want to be rid of their own local tyrant. The centre has also developed a conflict-simulation game that shows the effect of different tactics—strikes, demos, boycotts, etc—which can be tailored to particular circumstances.

All politics is local

Success has many fathers, and when people power turns out well many will claim the credit. Reasonably enough: the pressure of foreign governments, the activities of outside NGOs, moral support, financial help, the foreign press, the use of e-mails and so on have all contributed to the downfall of various dictators. But all the evidence is that people power, if it is to bring about a lasting change that increases freedom, must bubble up from below. It must be indigenous, broad-based and, ideally, non-violent. In practice, that means it must be organised, and led by people who could be plausible politicians after the revolt. And they must be on the spot: exiles carry little weight if they have sat out the struggle at a safe distance—a truth well understood by the Cubans, who fear a United States-shunning dissident like Oswaldo Payá far more than any ranter in Miami.

AFP

Iranians mustered but not quorate

Countries with few local NGOs, civic groups, trade unions, churches, student organisations or other independent sources of influence are unlikely to produce the necessary leaders. And if they do, the sensible autocrat will squelch them as soon as possible. That is what happens in Iran, where opponents of the regime, especially students, are given no chance to organise, and where television is always censored and newspapers often closed.

Yet people power still worries the world's authoritarians. The Chinese sent 10,000 policemen to a southern town last week to crush a demonstration that involved barely half as many participants. Thousands of similar protests have erupted across China recently, and the country's chief press regulator, Shi Zongyuan, unblushingly admitted in November: “When I think of the colour revolutions, I feel afraid.” Russia, too, is concerned: NGOs, says the head of its security service, are plotting to destabilise the country. A new law now restricts domestic ones and gives the government power to close down their foreign counterparts. Russia also harasses the American-backed agencies promoting democracy in Central Asia.

Plenty of other governments, from Belarus to Myanmar to Zimbabwe, are frightened. They are probably right to be. It may take years to develop, and it may not always turn out quite as is hoped, but people power is catching:

the more often it works, the more often it will be used.

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Higher education and the poor

Rebuilding the American dream machine

Jan 19th 2006 | NEW YORK
From The Economist print edition

Getty Images

A parable of elitism in universities

FOR America's colleges, January is a month of reckoning. Most applications for the next academic year beginning in the autumn have to be made by the end of December, so a university's popularity is put to an objective standard: how many people want to attend. One of the more unlikely offices to have been flooded with mail is that of the City University of New York (CUNY), a public college that lacks, among other things, a famous sports team, bucolic campuses and raucous parties (it doesn't even have dorms), and, until recently, academic credibility.

A primary draw at CUNY is a programme for particularly clever students, launched in 2001. Some 1,100 of the 60,000 students at CUNY's five top schools receive a rare thing in the costly world of American colleges: free education. Those accepted by CUNY's honours programme pay no tuition fees; instead they receive a stipend of $7,500 (to help with general expenses) and a laptop computer. Applications for early admissions into next year's programme are up 70%.

Admission has nothing to do with being an athlete, or a child of an alumnus, or having an influential sponsor, or being a member of a particularly aggrieved ethnic group—criteria that are increasingly important at America's elite colleges. Most of the students who apply to the honours programme come from relatively poor families, many of them immigrant ones. All that CUNY demands is that these students be diligent and clever.

Last year, the average standardised test score of this group was in the top 7% in the country. Among the rest of CUNY's students averages are lower, but they are now just breaking into the top third (compared with the bottom third in 1997). CUNY does not appear alongside Harvard and Stanford on lists of America's top colleges, but its recent transformation offers a neat parable of meritocracy revisited.

Until the 1960s, a good case could be made that the best deal in American tertiary education was to be found not in Cambridge or Palo Alto, but in Harlem, at a small public school called City College, the core of CUNY. America's

first free municipal university, founded in 1847, offered its services to everyone bright enough to meet its gruelling standards.

City's golden era came in the last century, when America's best known colleges restricted the number of Jewish students they would admit at exactly the time when New York was teeming with the bright children of poor Jewish immigrants. In 1933-54 City produced nine future Nobel laureates, including the 2005 winner for economics, Robert Aumann (who graduated in 1950); Hunter, its affiliated former women's college, produced two, and a sister branch in Brooklyn produced one. City educated Felix Frankfurter, a pivotal figure on the Supreme Court (class of 1902), Ira Gershwin (1918), Jonas Salk, the inventor of the polio vaccine (1934) and Robert Kahn, an architect of the internet (1960). A left-wing place in the 1930s and 1940s, City spawned many of the neo-conservative intellectuals who would later swing to the right, such as Irving Kristol (class of 1940, extra-curricular activity: anti-war club), Daniel Bell and Nathan Glazer.

What went wrong? Put simply, City dropped its standards. It was partly to do with demography, partly to do with earnest muddleheadedness. In the 1960s, universities across the country faced intense pressure to admit more minority students. Although City was open to all races, only a small number of black and Hispanic students passed the strict tests (including a future secretary of state, Colin Powell). That, critics decided, could not be squared with City's mission to “serve all the citizens of New York”. At first the standards were tweaked, but this was not enough, and in 1969 massive student protests shut down City's campus for two weeks. Faced with upheaval, City scrapped its admissions standards altogether. By 1970, almost any student who graduated from New York's high schools could attend.

The quality of education collapsed. At first, with no barrier to entry, enrolment climbed, but in 1976 the city of New York, which was then in effect bankrupt, forced CUNY to impose tuition fees. An era of free education was over, and a university which had once served such a distinct purpose joined the muddle of America's lower-end education.

By 1997, seven out of ten first-year students in the CUNY system were failing at least one remedial test in reading, writing or maths (meaning that they had not learnt it to high-school standard). A report commissioned by the city in 1999 concluded that “Central to CUNY's historic mission is a commitment to provide broad access, but its students' high drop-out rates and low graduation rates raise the question: ‘Access to what?’ ”

Using the report as ammunition, profound reforms were pushed through by New York's then mayor, Rudolph Giuliani, and another alumnus, Herman Badillo (1951), America's first Puerto Rican congressman. A new head of CUNY was appointed. Matthew Goldstein, a mathematician (1963), has shifted the focus back towards higher standards amid considerable controversy.

For instance, by 2001, all of CUNY's 11 “senior” colleges (ie, ones that offer full four-year courses) had stopped offering remedial education. This prompted howls from the teaching faculty, who said it would “create a ghetto-like separation between levels of colleges”, keeping black and Hispanic students out of the best schools. In fact, the racial composition of the senior schools, monitored obsessively by critics, has remained largely unchanged: one in four students at the senior colleges is black, one in five is Latino. A third have ties to Puerto Rico, Jamaica, China and the Dominican Republic.

Admissions standards have been raised. Students applying to CUNY's senior colleges now need respectable scores on either a national, state or CUNY test, and the admissions criteria for the honours programme are the toughest in the university's history. Contrary to what Mr Goldstein's critics predicted, higher standards have attracted more students, not fewer: this year, enrolment at CUNY is at a record high. There are also anecdotal signs that CUNY is once again picking up bright locals, especially in science. One advanced biology class at City now has twice as many students as it did in the late 1990s. Last year, two students, both born in the Soviet Union, won Rhodes scholarships, and a Bronx native who won the much sought-after Intel Science Prize is now in the honours programme.

All this should not imply that CUNY is out of the woods. Much of it looks run down. CUNY's annual budget of $1.7 billion has stayed largely unchanged, even as student numbers have risen. With New York City's finances still precarious, city and state support for the university has fallen by more than one-third since 1991 in real terms. It has, however, begun to bring in private money.

A new journalism school will open in the autumn, helped by a $4m grant from the Sulzberger family, who control the *New York Times*, and led by *Business Week*'s former editor, Steve Shepard (class of 1961). Efforts to raise a $1.2 billion endowment have passed the half-way mark, helped by (formerly estranged) alumni. Intel's former chairman, Andrew Grove, who graduated from City in 1960 as a penniless Hungarian immigrant, donated $26m (about 30% of City's operating budget) to the engineering school, calling his alma mater “a veritable American dream machine”.

There are broader lessons to draw from CUNY, especially to do with creating opportunities in higher education for the poor. Currently, only 3% of the students in America's top colleges come from families in the lowest income quartile and only 10% from the bottom half, according to a study by Anthony Carnevale and Stephen Rose for the Century Foundation. Most students are relatively well-off, and their numbers include plenty of racial minorities who receive preferential status independent of their economic circumstances.

For all its imperfections, CUNY's model of low tuition fees and high standards offers a different approach. And its recent history may help to dispel the myth that high academic standards deter students and donors. “Elitism”, Mr Goldstein contends, “is not a dirty word.”

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WORLD
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New Orleans

The Big not-quite-so-Easy

Jan 19th 2006 | NEW ORLEANS
From The Economist print edition

AP

Life in the Lower Ninth

A smaller, safer New Orleans makes sense. It may not come to pass

IN PARTS of the Lower Ninth Ward, people who want to rebuild their houses will have to find their land first. When the levees enclosing the Industrial Canal failed during Hurricane Katrina last August, most of this poor black neighbourhood disappeared. Its most prominent landmark is now a hulking barge that escaped from the canal and lies stranded in a wasteland. Farther away from the levee breach, buildings still look like buildings; but they have been ripped off their foundations and tangled up with other structures. Apart from a few carloads of gawkers and an encampment of earnest students, the area is devoid of life.

It may never revivify. Under a plan put forward by Mayor Ray Nagin's Bring New Orleans Back Commission (BNOB), areas that experienced minimal flooding by Katrina would be rebuilt immediately. But residents in the harder hit areas, such as the Lower Ninth Ward (which was also hammered by Hurricane Betsy in 1965), would have until May 20th to show that they would return in sufficient numbers to keep their neighbourhoods alive. If they fail to do so, homeowners could be “bought out” in some way and the areas in question could revert to swampland or be turned into parks.

A mass migration to higher ground would appear to make sense—and not just because nobody wants a repeat of last summer's disaster. For the foreseeable future, New Orleans will be a smaller city. The city's population, which rose above 600,000 in the mid-1960s, had declined to about 462,000 before Katrina emptied the town. The mayor's commission puts the current figure at 144,000, but expects the population to be only 247,000 by 2008.

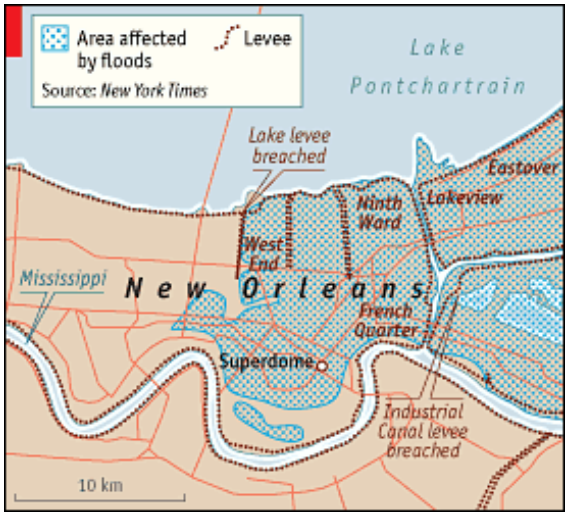
Even before the hurricane, city agencies struggled to fight crime, mow grass and keep streets and waterpipes in working order. After losing much of its tax base, New Orleans may be too broke to provide services over the same geographical area. The cost of subsidising services for a few foolhardy souls could be better spent in potentially viable neighbourhoods. Most urban planners insist that the city must write off some areas for the rest to survive.

Here, however, logic runs into principle and racial politics. Many politicians feel queasy about violating the property rights of individual householders, some of whom are determined to return to their homes come what may. There are also accusations of racism. Most of the city's highest neighbourhoods are also its oldest, wealthiest and whitest. There are some exceptions—Lakeview, a rich white area, and Eastover, a rich black one, were both hit hard—but, in general, plans to shrink the city's size could mean the end of a lot of poor black neighbourhoods.

God and chocolate fudge

The city council has passed a resolution urging the immediate and equal redevelopment of all parts of the city. This looks like grandstanding. The resolution is non-binding and it is not clear who would pay for it. The Bush administration has agreed to pay for new pumping stations along Lake Pontchartrain and the closure of three drainage canals—steps that could improve the safety of areas west of the Industrial Canal. But eastern New Orleans and the Lower Ninth Ward may not be protected for years.

Inevitably, the rebuilders at BNOB have tried to put off the decision. One of its leaders, Joseph Canizaro, a property developer (and Republican fund-raiser), suggested reopening all the city to development and then deciding in three years which bits to close down. Others wanted to wait for a year, which would also have left householders unsure whether to rebuild.



The current proposal, the four-month waiting period, was a compromise. It includes a moratorium on building permits in the hard-hit areas until the decision is made—a crucial component in a city that has already issued thousands of permits and is issuing more than 100 a day.

Public officials in Louisiana tend to be chosen for their ability to bring home the pork, rather than in telling angry people what they don't want to hear. This week, the sometimes eccentric Mr Nagin called Katrina a sign that “God is mad at America” and promised that he would fulfil the Almighty's wish that New Orleans be rebuilt as a “chocolate” city with a majority black population. But he has not yet said whether he will abide by the BNOB recommendations. State officials are also mum on this subject—as is George Bush.

In this political vacuum, most of the news is coming from victims in the worst-hit areas. Signs of discord are evident. “I don't know you, but I hate you,” a resident of eastern New Orleans told Mr Canizaro at a meeting. Community activists have sued to keep the city from bulldozing in the Lower Ninth Ward. Shots were fired at a march called to show civic unity.

In the end the decisive vote in New Orleans will come not from those householders who are determined to return but from those who are currently unsure whether to rebuild or move on. Many of them owe more on their mortgages than their homes are worth. If they cannot extricate themselves, many will have to stay. Hence the interest in a bill sponsored by Richard Baker, a Republican congressman from Baton Rouge, who wants Congress to create a recovery corporation that would buy out the owners of ruined homes.

This could be hugely expensive: the corporation could issue up to $30 billion in bonds. But at least Mr Baker and BNOB, like the Almighty (as revealed to Mr Nagin), have come up with a plan. Unless other politicians are prepared to make some hard, expensive decisions, the Big Easy's future looks chaotic.

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Death and the law (1)

The court approves

Jan 19th 2006 | SEATTLE
From The Economist print edition

Oregon's assisted-suicide law survives—for now

ON A November day in 1999, Frederick Miller, terminally ill with lung and brain cancer, ate a bowl of apple sauce laced with barbiturates. Ninety minutes later, with his wife Nora by his side, the 52-year-old died peacefully.

That scene occurred in Portland, Oregon, where since 1997 it has been legal for a doctor to prescribe a fatal cocktail of drugs to patients who are terminally ill. But that law, the Death with Dignity Act, has been hotly debated for most of its existence. In 2001 John Ashcroft, then attorney-general of the United States, claimed that prescribing drugs to end life was not a “legitimate medical purpose”. This started legal skirmishing that landed the Oregon law before the Supreme Court. But for the moment the option to take one's own life, with a doctor's help, stays open. On January 17th the Supreme Court ruled 6-3 that Oregon could keep its assisted-suicide law.

The decision depended largely on whether states or the federal government should control how doctors do their work. The majority of justices decided that states should. But for most people, including the dissenting judges, the legal technicalities were secondary to the bigger question of whether doctors ought to help people end their lives.

Opponents of Oregon's law insist that it is simply legalised murder. Others see the law as appropriate, even enlightened, giving dying patients a much-needed choice when heroic medical procedures cannot help. “It's not as if [physician-assisted suicide] isn't happening elsewhere in the country,” says Timothy Quill, a doctor and professor at the University of Rochester in New York. “But in Oregon it's out in the open, so you don't have patients asking questions in secret, and doctors giving advice in secret.”

Another supporter, Arthur Caplan, the director of the Centre for Bioethics at the University of Pennsylvania, says there is no evidence that Oregon's law has been used to “kill” anyone: “Critics have been desperate to find someone who [took fatal drugs] and was imbalanced or not terminally ill, but they haven't been able to.” He points to the prudence exhibited by Oregonians, with only 238 people using prescribed drugs to end their lives (though for those who regard life as sacred that is still 238 too many).

For those who use Oregon's law and their survivors—such as Frederick Miller's widow, Nora—the Death with Dignity Act simply makes sense. Her sister recently died of cancer in Florida, an experience more painful and emotionally wearing than Frederick's planned death. “When Rick died he was calm and comfortable,” says Ms Miller, who now lives in Phoenix. “When he took the drugs his body was ready, and he fell deeply asleep almost immediately. I just hope I have that option, if I need it, when the time comes.”

Whether Oregon's law will gain traction nationally remains to be seen. Vermont, California and Washington state want to follow suit. But a future challenge in the Supreme Court could face a different outcome, as the three justices who dissented strongly from the majority—Antonin Scalia, Clarence Thomas and John Roberts, the new chief justice—will probably be joined soon by a like-minded fellow-Catholic, Samuel Alito. That probably turns a comfortable 6-3 margin into a much tighter 5-4 one. Another conservative nomination could give opponents of the Oregon measure an edge. Beyond that, says Mr Caplan, distrust of the medical profession is currently running so high—pushed by rising costs, the perceived greed of some health-care bosses and malpractice suits—that not many state voters will readily give doctors the same responsibility they have in Oregon.

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Death and the law (2)

A matter of evidence

Jan 19th 2006 | RICHMOND
From The Economist print edition

A 76-year-old is executed and the hunt for a proven innocent goes on

AP

Coleman was guilty

NEARLY 14 years ago a Virginian coal miner was executed in the electric chair for the rape and murder of his sister-in-law. To his last breath, Roger Keith Coleman swore he was innocent—and his cause has been taken up by death-penalty opponents ever since. On January 12th, DNA tests proved he was guilty. A few days later, with appeals to the Supreme Court and Governor Arnold Schwarzenegger both rejected, Clarence Ray Allen, a blind, diabetic 76-year-old convicted of having three people killed, including his son's girlfriend, was helped from his wheelchair and put to death by lethal injection in California.

The victory for death-penalty supporters may not have been as complete as it seems. In their appeals to the Supreme Court, Mr Allen's lawyers tried to establish that his execution would constitute “cruel and unusual punishment” on two new grounds: first, because he was so old (he was the second-oldest to be executed, behind a 77-year-old in Mississippi last month); and, second, because he had spent so long on death row—23 years. Neither convinced the court, but Justice Stephen Breyer said Mr Allen's case raised important questions.

The Coleman case offered death-penalty opponents the chance to prove scientifically that an innocent man had been murdered by the state. More than 100 people on death row have been exonerated of the crimes for which they were convicted; but none of the 1,005 people who have been executed since capital punishment was reinstated in 1976 has been proved conclusively innocent using DNA. The apparently firm proof of Coleman's guilt—a scientist still had a swab from the victim—was “a kick in the stomach”, as one Coleman supporter put it.

However, it hardly ends the debate. Several other cases around the country look extremely murky. And the Coleman case did break ground in one way: it was the first time that a governor had ordered a DNA test for a man already put to death. Mark Warner, the outgoing Democratic governor (who supports the death penalty), is now angling for his party's presidential nomination in 2008. Cynics claimed his decision to order the tests was a way to suck up to liberal activists who otherwise might not look too warmly on a governor who had overseen the execution of 11 people.

But Mr Warner also had other concerns. Two years ago, revelations of flawed DNA tests by the state's nationally recognised crime laboratory threatened confidence in law enforcement. A retarded man, ultimately proved innocent by independent genetic examination, had come within days of execution. He was pardoned in 2000, though he had to wait another four years until he was fully exonerated by science.

Earlier this month, New Jersey put a moratorium on executions. In Virginia, the Republican-controlled legislature, returning to work just as Mr Warner relinquished the governorship, rejected a proposal to follow suit. The new governor, Timothy Kaine, once favoured such a freeze. But he has changed his mind, partly because he thinks that DNA evidence increasingly provides certainty.

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WORLD
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Republicans in New York

Mike, you stay and turn the lights off

Jan 19th 2006 | NEW YORK
From The Economist print edition

A state party facing a very tough year

IF THE first duty of a politician is to get elected, New York's Republicans look set to fail their voters badly this year. They have yet to agree on a candidate for governor in November's election, let alone one with much hope of beating the Democrat frontrunner, Eliot Spitzer. They have yet to agree also on a candidate to run (and lose) against Hillary Clinton when she seeks re-election to the Senate. A Republican might yet win the race to succeed Mr Spitzer as attorney-general, but even there things are going badly. The party's best hope, Jeanine Pirro, a former prosecutor from Westchester County, spoilt her credibility by starting and then abandoning a campaign for Mrs Clinton's seat late last year.

Factional rivalries contribute to the Republicans' disarray. Their retiring governor, George Pataki, was never a commanding figure within the party, and he seems to have lost himself now in thoughts of a presidential bid in 2008—an impression reinforced by his annual policy speech earlier this month, weighted much more to national than to local issues. His imminent departure, without an obvious heir, leaves two camps jostling locally for influence. On one side are Mr Pataki's loyalists, such as Stephen Minarik, chairman of the state Republican Committee. On the other are officials closer to Joseph Bruno, the veteran leader of the Republican majority in the state Senate, who stands to emerge as the party's de facto boss.

The Pataki camp wants William Weld, a former governor of Massachusetts, as its candidate for governor of New York. A Harvard-educated classicist, lawyer, *bon viveur*, novelist and Grateful Dead fan, Mr Weld is a clever and charming man with plenty of rich friends who could help raise campaign funds. But his social liberalism offends the party's right, and his reputation may be hurt by the collapse last year of a private college in Kentucky of which he was briefly the chief executive.

Mr Bruno is said to lean more towards Tom Golisano, a rich businessman from Rochester, who enrolled as a Republican in October after contesting the previous three governors' elections as a third-party candidate. Mr Golisano has said he will decide very soon whether to run again as a Republican. If he does, his money alone will guarantee him a fair measure of support. It will become hard for the Republicans to avoid a costly and distracting primary in September between Mr Golisano, Mr Weld and probably a third candidate, John Faso, a lawyer from Long Island who appeals to the right.

New York is hostile terrain for Republicans at the best of times. Registered Democrats outnumber them by five to three, and five to one within New York City. To win a statewide election at all, the Republicans need either a candidate capable of appealing to moderate Democrats, or a weak Democrat running against them, and preferably both. That was how Mr Pataki first got elected governor in 1994 (when voters grew tired of the windy Mario Cuomo), and how Rudy Giuliani and Michael Bloomberg got elected mayor of New York City in 1993 and 2001 respectively.

This year the Democrats have turned the tables. They are the ones with the glittering crossover candidates, in the shape of Mr Spitzer and Mrs Clinton. The former may yet be forced into a primary contest by a fast-rising young rival, Thomas Suozzi, chief executive of Nassau County, but Mr Spitzer's prospects look good. An opinion poll conducted by Quinnipiac University in mid-December found that 64% of Republicans thought he was doing a good job as attorney-general, scarcely less than his 72% approval rating among Democrats. As for Mrs Clinton, she may remain loathed by conservatives around the country, but in left-leaning New York everything is relative: 49% of voters consider her a “moderate” or “conservative” figure, including 28% of Republicans.

The problem with Albany Inc

To make life worse for the Republicans, they have a long-standing rival to the right in the form of the Conservative Party, founded in 1962 as a reaction against the social liberalism and big-spending habits of Nelson Rockefeller and other state Republican leaders. The Conservatives have only 155,000 registered voters against 3.2m Republicans. But the state's electoral law makes it relatively easy for minor parties to keep a line on the ballot paper in New York. If the Conservatives dislike a Republican candidate, they can run a competitor and divide the right's already small vote.

The Conservatives' endorsement gave Mr Pataki his margin of victory in 1994. At the time, the genial state senator was seen as a fiscal conservative. But he failed to make the necessary impact, according to a new report, “Albany Inc”, from the right-leaning Manhattan Institute. New York's government, it moans, “spends, taxes and borrows far more than the national average, consistently ranking at or near the top of the list in every measure of the burden that government imposes on citizens and businesses.” Mr Pataki did offer some modest tax cuts this week in his final state budget proposal, but most would take effect only after he left office.

Against this background, rallying support among conservatives for Mr Weld or Ms Pirro (and their liberal respective positions on abortion and gun control) will be hard. By the end of this year, Mr Bloomberg—a man who joined his current party only shortly before running for mayor and doesn't differ from Mrs Clinton on much— may be the only Republican of any note left in office in the state.

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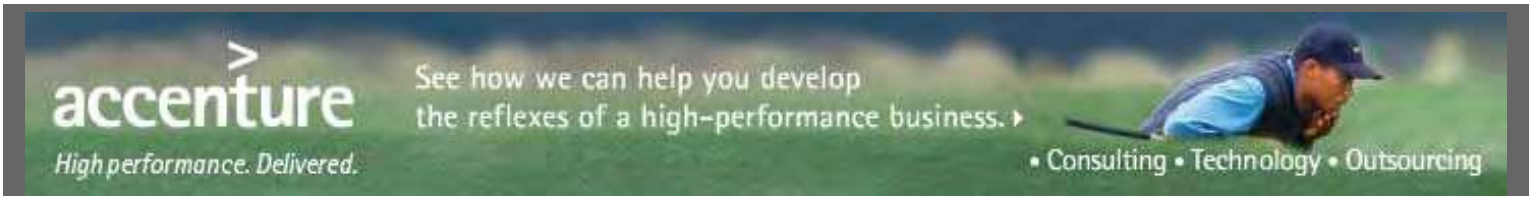
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Health care

This year's political punch-bag?

Jan 19th 2006
From The Economist print edition

Politicians in Maryland go shopping for an easy target

WAL-MART already dominates American retailing. Now it seems to be playing an ever-bigger role in its politics, too. Various councils have tried to ban the huge store from their towns, ostensibly to protect local shopkeepers. Now it is part of the increasingly fierce battle over health care and the Medicaid programme for the poor.

On January 12th, the Democrat-controlled legislature in Maryland passed a bill requiring any employer with more than 10,000 employees to spend at least 8% of its payroll on health care for its workers. If it spends less, it must give the difference to Maryland's Medicaid programme. The Republican governor, Robert Ehrlich, vetoed a similar effort in May last year; this time the majority is too big to be stopped by him.

The law is not actually called the Wal-Mart law, but it might as well be, as the Arkansas-based giant is the only company affected by it. The unions, who loathe Wal-Mart, claim that politicians in some 30 states are considering similar laws. The nation's largest private-sector employer provides health insurance to less than half of its 1.3m workers. This, argue its critics, is a problem not just for its employees, but also for state governments, because it is often their Medicaid programmes that wind up paying the workers' medical expenses.

Whatever the rights or wrongs of Wal-Mart's modus operandi, it is unclear whether bashing the company will help Maryland very much. To begin with, the bill may violate the federal Employment Retirement Income Security Act, which gives Congress the sole authority to regulate employee benefits. Even if the law is legal, Maryland won't save much money. By Wal-Mart's calculation, 786,000 residents of Maryland do not have health insurance; it employs only 17,000 people in the state.

The bigger problem with insurance has to do with small firms. According to the Chamber of Commerce, roughly 25m of the 46m uninsured Americans work for companies with ten or fewer employees. If politicians attacked them, uproar would follow. Besides, the main reason why Medicaid spending keeps rising is not stingy employers, but rising health-care costs. And now, since it must pay 8% of its payroll either way, Wal-Mart has little incentive to reduce its health costs in Maryland.

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Lexington

Match point for Doctor No

Jan 19th 2006
From The Economist print edition

This may be the right moment for a maverick senator from Oklahoma

“THERE are moments in a match when the ball hits the top of the net,” muses the anti-hero in “Match Point”, Woody Allen's best film in years. “And, for a split second, it can either go forward or fall back. With a little luck, it goes forward and you win...or maybe it doesn't and you lose.” Tom Coburn, the freshman senator from Oklahoma, could hardly be more unlike Mr Allen's tennis-playing rogue; he is a blunt-talking doctor who suffers from a surfeit of principles rather than a lack of them. But the metaphor of the tennis ball balanced delicately on the net perfectly captures his recent political career.

For some time it looked highly unlikely that Mr Coburn would win any points at all in the Senate. He is a maverick in an institution that puts a premium on conformity; a purist in an institution that puts a premium on compromise; and a straight-shooter on awkward subjects, such as sexually transmitted diseases, in an institution that puts a premium on politically correct platitudes. Above all, in a club where most members rather like the idea of using public money to buy public support and getting their name festooned on roads and sculpture parks, he spends much of his time attacking political pork.

Yet the past few months have transformed this pariah into a force to be reckoned with. Two things have tipped the doctor's ball over the net. The first is Hurricane Katrina, which gave him a chance to renew his attack on the $286 billion transport bill. How could Congress justify spending $24 billion on “earmarks” at a time of national emergency? (Earmarks, for the uninitiated, are spending projects that are directly requested by individual members of Congress and are not subject to competitive bidding.) And how could it justify spending $223m on a “bridge to nowhere” in Alaska when New Orleans was under water?

Mr Coburn did not stop the bridge, and he lost more friends. Ted Stevens, the senior senator for Alaska and the former chairman of the appropriations committee, implied that he had never been so insulted in his 37 years in Congress (which is a pity). But Mr Coburn won the argument: he turned “the bridge to nowhere” into a symbol of waste and corruption.

The second thing that has redeemed Mr Coburn is the Abramoff lobbying scandal. Lobbyists love earmarks: they are a way to smuggle pet projects into vast spending bills without even the pretence of proper oversight. It is no coincidence that the supersizing of the lobbying industry has coincided with the multiplication of earmarks. And it is

no coincidence that the most egregious examples of lobbying corruption involve earmarks. Randy “Duke” Cunningham, a former congressman from California, admitted taking $2.4m in bribes in exchange for earmarks. Mr Abramoff bragged that appropriations committees were “earmark favour factories”.

Mr Coburn has been making his case against earmarks for a decade, but now he can command a national audience. He argues that earmarks make it impossible for politicians to prioritise: they explain why the New Orleans levees were allowed to crumble but money was appropriated for unnecessary bridges. They also encourage a culture of spending. Legislators vote for bloated spending bills—such as the prescription-drug benefit bill—in order to get their earmarks through and they also engage in cynical “I'll vote for your earmarks if you vote for mine” horsetrading. And he laments that earmarks are hopelessly addictive. The number of pork projects has increased by 970% in the past ten years. Mr Coburn has called for the elimination of earmarking to be the centrepiece of any post-Abramoff reforms in Congress, and pledged to force his colleagues to justify their earmarks on the floor of the Senate.

The deliverer of bad tidings

There are all sorts of reasons why he might fail. The establishment will surely hit back hard, and the good doctor offers plenty of targets. He is on record worrying about “rampant” lesbianism in Oklahoma schools, supporting the death penalty for abortionists and claiming that the gay agenda “is the greatest threat to our freedom that we face today”. He made lots of enemies in his six years in the House. Fellow Republicans have called him a “burr under the saddle of the party”; Dennis Hastert, the House Speaker, publicly predicted that Mr Coburn would lose his Senate race.

But Mr Coburn is no longer quite so isolated. The rumble of discontent with pork-barrel spending has won him support from across the political spectrum, from big-government liberals as well as anti-government conservatives. In this battle, powerful Republicans such as Sam Brownback and John McCain are on his side. Jeff Flake, a congressman from Arizona, wants to subject all earmarks to debate and amendment. It is a measure of how far the anti-pork campaign has got that John Boehner, a candidate for the House leadership and an establishment man if ever there was one, recently penned an article for the *Wall Street Journal* calling for a “lower-pork diet”.

And Mr Coburn's singular personality in this instance may help. Put simply, it is hard to see him being bought off. It is not just that he regards the fact that he has survived two bouts of cancer as proof that God has special work for him; he has no intention of becoming a career politician. He wants to return to his preferred profession of medicine once he has served two terms. He delivered 400 babies while in the House and would still spend his weekends pulling them out if the Senate Ethics Committee hadn't decided that the profession of delivering babies was incompatible with the profession of kissing them.

In 1999, Mr Coburn brought the House to a virtual standstill by threatening to attach 130 amendments to a bloated agriculture bill. Let us hope that he will earn an even worse reputation in the Senate.

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WORLD
NORTH AMERICA

Canada's election

Harper glides past Martin and towards power

Jan 19th 2006 | OTTAWA
From The Economist print edition

The Conservative leader's move to the centre, and the Liberals' weary bungling, have combined to change the political landscape

AT THE end of November, when the Conservative opposition forced a confidence vote that toppled the Liberal minority government, the conventional wisdom in Ottawa was that the resulting general election would be pointless as well as untimely. The assumption was that the federal parliament to be elected on January 23rd would be much like the old one, not least because Canadians would not take kindly to a winter campaign.

But Stephen Harper, the Conservative leader, apparently knew better. As the campaign drew to a close, the only question was whether he would win power with an outright majority or at the head of a Conservative minority government. Recent polls gave the Conservatives between 37% and 41%, against 24% to 32% for the Liberals, 16% to 20% for the leftish New Democrats (NDP) and 11% for the separatist Bloc Québécois. They suggested the Conservatives might win anything from 130 to 152 of the 308 seats in the House of Commons.

Barring a last-minute reversal in their fortunes, the Conservatives looked set to make massive inroads in Ontario, a Liberal stronghold with almost 40% of the electorate. They were even poised to win seats in Quebec, where Conservatism has been almost extinct, as federalists switched from the Liberals. That might frustrate the Bloc's earlier hopes of taking 50% of the vote, which its supporters would use as an argument for another referendum on independence in the French-speaking province. However, a three-way fight in a first-past-the-post electoral system could help the Bloc to add to its 54 seats.

In taking the Conservatives to the brink of power for the first time since 1993, Mr Harper has tapped a new political mood. He has done so in part through his own ruthless decision to move the Conservatives to the political centre on a host of issues. He has been helped by the bumbling, bungling weariness of the Liberals and of Paul Martin, the prime minister.

Mr Harper, a 46-year old economist and passionate fan of ice-hockey, cut his political teeth on the libertarian right. Though born in Toronto, he moved to oil-rich Alberta as a young man. There he formed part of a group which broke from the Progressive Conservatives of Brian Mulroney, the prime minister from 1984-93, over what they

perceived as his fiscal laxity and his cosseting of French-speaking Quebec. They founded the Reform Party (later the Alliance), which by splitting the right guaranteed it more than a decade in the political wilderness.

In 2003, Mr Harper brokered an uneasy marriage between the Alliance and the rump of the Progressive Conservatives to form a new Conservative Party. At a general election in June 2004, the Conservatives took an early lead in the polls. But Mr Martin squeaked home after the Liberals found it easy to paint Mr Harper as an extreme social conservative.

Not this time. Mr Harper has crafted an effective blend of traditional conservatism and reassuring moderation. His promises to be tough on crime, cut the sales tax and boost defence spending have played well in suburban Ontario. But he has also pledged to uphold the national health service, ruled out any change in Canada's abortion law, and tempered his party's previous opposition to gay marriage and the Kyoto climate protocol.

If Mr Harper is winning the campaign, the Liberals have done even more to lose it. For years a successful finance minister under Jean Chrétien, Mr Martin has disappointed as prime minister since 2003. He failed to land any blows in the televised debates among the party leaders. An attempt to embarrass Mr Harper misfired when the prime minister, without consulting his own party's constitutional experts, abruptly offered to renounce a provision that allows the federal government to override Supreme Court decisions.

In mid-campaign, the police launched an investigation into insider trading following the leaking of an announcement to be made by the finance minister. That served to remind voters of past episodes of Liberal sleaze, and of what a recent judicial investigation called their “culture of entitlement”. The Liberals' “attack ads” have blown up in their faces. One spot, published on a web-page though not broadcast, twisted Mr Harper's plan to station small army units in cities in readiness for floods and disasters into something akin to a military coup. That angered veterans and brought ridicule on the Liberals.

In 2004, Mr Martin persuaded some voters to back the Liberals rather than the New Democrats as the only way to stop the Conservatives. That argument is unlikely to wash this time. Instead, Jack Layton, the NDP leader, hopes to attract disillusioned Liberals.

Mr Harper is not yet home and dry. If he fails to win a majority, he might have to depend on the Bloc. That could involve big fiscal concessions to the provinces, and a return to the federal deficits ended by Mr Martin when finance minister. The prospect of a Conservative majority might frighten some swing voters who doubt the sincerity of Mr Harper's move to the centre. But in the final days of campaigning, with Mr Harper concentrating on Quebec and Mr Martin criss-crossing the country, it looked as if the long era of Liberal domination was drawing to a close.

The *Globe and Mail*, a middle-of-the-road newspaper, summed up the new mood in an editorial when it swallowed its reservations and endorsed the Conservatives. “Today, Canadians clearly are ready for change. If not now—if not after a painfully incoherent minority Liberal government, if not after a succession of scandals, if not after four full terms of deteriorating government—then when?”

All this will doubtless be noted in Britain. A victory for Mr Harper will give heart to David Cameron, another Conservative leader leading his party to the centre. It might also strike fear into Gordon Brown, a successful finance minister hoping to elbow aside a long-serving prime minister, just as Mr Martin did Mr Chrétien.

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Bolivia

Enter the man in the stripey jumper

Jan 19th 2006 | LA PAZ
From The Economist print edition

Evo Morales's "democratic revolution" is kicking off with mixed messages

Get article background

AP

Not just a fashion victim

IT PROMISES to be a presidential inauguration like no other since Bolivia returned to democracy in the 1980s. For a start, Evo Morales, the new president, is unlikely to wear a suit and tie for the occasion on January 22nd. His recent world tour, taking in eight countries, was memorable not so much for his sometimes erratic rhetoric as for his skilful creation of a personal fashion style. This featured a distinctive red, grey, blue and white striped jersey, worn when he met the king of Spain and the president of China.

More importantly, Mr Morales, Bolivia's first president to proclaim his indigenous origins, has a powerful mandate. He will be the fourth president of his unstable country in less than three years, but the first since democracy was restored to have won an absolute majority. His Movement Toward Socialism (MAS) captured a majority of the lower house of Congress. It fell just short in the Senate, but looks likely to get its way there too.

To many Bolivians, the electoral triumph of Mr Morales, a coca-growers' leader and political street fighter, amounts to a "democratic revolution". The traditional parties that governed Bolivia for the past two decades were all but wiped out. Just 17 of the 157 members of the newly elected Congress are survivors from the previous one.

Before the vote, Mr Morales scared foreign energy companies, Bolivia's biggest investors, by calling for nationalisation of gas; he irritated the United States by opposing the forced eradication of coca; he terrified businessmen in Bolivia's rich eastern provinces by promising land reform and state control of the economy. These tensions have not disappeared, but the scale of Mr Morales's victory, and his shrewd use of it, have eased them, for now.

On his tour, he gave two different messages. With Hugo Chávez in Venezuela, he denounced "neoliberalism" and "imperialism". In return, his host promised to swap Venezuelan oil for Bolivia's soya and to provide $30m of launch aid to Mr Morales's government.

But Mr Morales also showed pragmatism. In Brazil and Spain, home to the two biggest investors in Bolivian gas, he declared that nationalisation did not mean expropriation and promised security of contracts. Brazil's state-owned Petrobras said it would become a partner of YPFB, the dormant state energy company that Mr Morales wants to revive. The "anti-imperialist" called for relations with the United States "based on respect" and met the American ambassador. He cancelled a visit to Iran, an American nemesis.

If the trip showed Mr Morales's disposition to negotiate, he can do so from a position of strength—and not just because his neighbours covet Bolivia's gas. For a country that has looked deeply divided, Bolivia produced a surprisingly united election result. He won votes not just from the poor and Andean Indians, but in the more prosperous east and among *mestizos* (people of mixed race) fed up with the corruption of traditional political parties. Many apparently calculated that handing Mr Morales a decisive victory would make Bolivia more governable. This confers on the new president and Congress a legitimacy their recent predecessors lacked.

Although Mr Morales's victory has released the energy of an earthquake, Bolivia's fault lines remain. His base is in

the social movements, a loose coalition of indigenous groups, trade unions and civic organisations. He has promised them the moon. Gas will be nationalised. The minimum wage will be tripled to 1,500 bolivianos ($187.50) a month. A constituent assembly will “refound” Bolivia, in part by redistributing land in the prosperous east. Coca eradication will end.

Ranged against this utopian agenda is a collection of Bolivian and foreign interests. Also elected in December, for the first time, were nine *prefectos* (provincial governors) of whom only three belong to MAS. The *prefectos* of eastern provinces such as soya-growing Santa Cruz and gas-rich Tarija want a referendum on autonomy, to which Mr Morales has agreed. The crunch will come when they seek to shield themselves from land reform and to take control of health and education, a measure that trade unions will resist.

Then there are the talks with the gas companies, in which the government will have to reconcile its banner of nationalisation with the need to attract new investment. Even trickier will be relations with the United States. Its biggest worry, shared by Brazil and the European Union, is that the new government will give free rein to coca production. The head of Bolivia's army was sacked on January 17th, after he said that he had yielded to American pressure to send some 30 ageing Chinese surface-to-air missiles to the United States for destruction ahead of the election—an act that Mr Morales called “treason”.

Foreign aid, most of it from the United States or from institutions under its influence, accounts for a tenth of Bolivia's GDP. American trade preferences, due to expire at the end of the year, encourage the factory jobs the country needs to wean itself from dependence on natural resources. It is in Mr Morales's interests—but against his instincts—to secure and augment those jobs with a free-trade agreement.

He takes office with more diplomatic flair and a bigger stock of political capital than anyone expected. The next test will be to choose ministers who can translate his promises into workable policies. Fail, and the frustration on the streets may build again.

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WORLD
LATIN AMERICA

Michelle Bachelet

Doing it her way

Jan 19th 2006 | SANTIAGO
From The Economist print edition

Chile's new president promises continuity and change

Reuters

Get article background

Warm heart, now for cool head

IN MORE ways than one, the victory of Michelle Bachelet in a presidential election on January 15th symbolises the new self-confidence of Chile's democracy. Ms Bachelet is only the third woman to be elected to the top job in Latin America, and the first who was not the widow of an illustrious husband. She is the twice separated mother of three children in a country long considered socially conservative. And she is the daughter of an air-force general who died of a heart attack after being arrested by General Augusto Pinochet's dictatorship, and was herself briefly detained after his 1973 coup.

But Ms Bachelet, who defeated Sebastián Piñera, a conservative businessman, by 53.5% to 46.5%, embodies continuity as well as change. She will head the fourth consecutive government of the centre-left Concertación coalition. A moderate socialist, she says she will maintain the economic discipline and respect for markets that have sustained Chile's rapid growth of the past two decades.

She was more fiscally cautious in her election promises than Mr Piñera. She will retain the counter-cyclical fiscal rule established by the outgoing government of Ricardo Lagos. This mandates a fiscal surplus of 1% of GDP when the economy is growing at its potential (as defined by an independent panel of experts) and when the price of copper, Chile's main export, is at its expected long-term average.

Again echoing Mr Lagos, Ms Bachelet promises to do more to tackle inequality. She wants to guarantee access to pre-school education, and create new child-care schemes. To tackle youth unemployment of 20%, she plans a subsidy for firms which hire youths from poor families. More importantly, she may also tweak rigid labour laws, though only cautiously, to help students get part-time jobs.

Her main effort will be to overhaul Chile's much-hyped private pension system. Studies suggest that more than 50% of workers may not receive a decent pension, because of shortfalls in contributions.

Above all Ms Bachelet has promised more open government when she takes office on March 11th. “I want to be remembered not only for what I do, but also for how I do it,” she says. For instance, she plans to set up an independent committee on pension reform, which would consult ordinary citizens as well as experts.

Thanks to a constitutional reform cutting the presidential term by two years, she only has four years in which to do all this. She will have to overcome a relative lack of experience—having entered frontline politics late, she was minister of health and then defence. Unlike her predecessors, she will have a majority in the Senate, as well as the lower house of Congress. But she will have to negotiate legislation with the Concertación's constituent parties.

They contain many politicians with experience of that kind of horsetrading. But Ms Bachelet has promised many fresh faces in a cabinet half of whose members, she says, will be women. That is a risk. Her personal warmth has won her many friends. Whether her election will indeed presage further change in Chile's democracy, and more women in politics, depends on how effectively she governs.

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WORLD
LATIN AMERICA

Trade politics in South America

A threat to defect

Jan 19th 2006 | SÃO PAULO
From The Economist print edition

Uruguay challenges its big neighbours by flirting with the United States

IS MERCOSUR expanding or contracting? The South American trade group dominated by Brazil and Argentina recently agreed to admit Venezuela as a fifth full member and may extend a similar invitation to Bolivia. Now Uruguay, Mercosur's smallest member but its most solid democracy, is casting glances at the exit. This month Danilo Astori, the economy minister, said that a free-trade agreement with the United States could “generate significant increases” in economic growth. Brazil and Argentina, he complained, are damaging Mercosur's smaller members by rejecting the idea. Another minister echoed the call for bilateral talks with the United States. If these went ahead, some argue that Uruguay would have to leave Mercosur.

This is a shock. Tabaré Vázquez, Uruguay's president, has been a fan of Mercosur and sceptical of the wider Free Trade Area of the Americas backed by the United States. Now Uruguay is echoing the discontent of Paraguay, the other Mercosur minnow, which complains that access to Brazil's market is theoretical. Uruguay's asperity has been sharpened by continuing protests in Argentina against two big paper projects, which critics claim will pollute rivers.

Uruguay may be bluffing. The United States might not want to antagonise Brazil by appearing to prise off one of Mercosur's founding members. Threatening to defect may be Uruguay's way of demanding better treatment from its Mercosur partners, argues Fernando González Guyer of the Mercosur Research Network in Montevideo.

Argentina and Brazil are starting to listen. On January 18th, Argentina's president, Néstor Kirchner, met his Brazilian counterpart, Luiz Inácio Lula da Silva, and confessed that Mercosur's smaller partners had suffered from “inattention”. Yet their meeting did little to advance a group whose common rules and tariffs are riddled with exceptions, barriers and disputes. Two of the items they discussed would limit integration rather than promote it: establishing safeguards, which would allow members to block imports from Mercosur partners in some circumstances, and extending an agreement to limit exports of Brazilian cars to Argentina. Mercosur may not shrink, but it is not thriving.

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Pakistan

Musharraf's unhappy new year

Jan 19th 2006 | LAHORE
From The Economist print edition

Troubles are piling up for Pakistan's president

Get article background

FOR Pervez Musharraf, Pakistan's president, troubles are coming not as single spies but in battalions. An American rocket attack on January 13th on a remote mountain village in Bajaur, a tribal agency near the border with Afghanistan, provoked angry nation-wide protests. Army action in Baluchistan province against rebellious tribesmen continues to take a toll of soldiers and civilians, and this week anonymous threats prompted foreign aid organisations to suspend operations there. Pakistan-controlled Kashmir, devastated by an earthquake in October, is suffering the misery of a Himalayan winter. Many Pakistanis fear the peace process with India is going nowhere (see article). To cap it all, the president has faced a political rebellion in Sindh province.

The strike in Bajaur was aimed at Ayman al-Zawahiri, the deputy leader of al-Qaeda, mistakenly thought to be there. It is reported to have killed three or four al-Qaeda terrorists—including an explosives expert on the most-wanted list—but also 18 civilians, including women and children. Pakistan has complained, but not over-loudly, given the presumed existence of secret agreements allowing America to wage war on Pakistani soil in certain extreme circumstances.

For the past three years, Pakistan's army has faced an uphill task in this mountainous area. It is infested with heavily armed Taliban and al-Qaeda remnants, bent on making trouble in Afghanistan. Hardly a day goes by without killings by both sides. On January 10th, for instance, seven soldiers and 14 “terrorists” died in clashes in the tribal areas. Locals sympathise with the militants and see the army as an intruder, there at the behest of the Americans. The army commanders say they have killed hundreds of foreign fighters, and frequently claim that the job is almost done. But that is not the case.

As if his troubles in the tribal areas and Baluchistan were not enough, General Musharraf has antagonised Sindh province by promoting the construction of a dam on the Indus river at a place called Kalabagh in Punjab. Sindh, further downstream, is bitterly opposed to the project. Such is the lack of trust that Sindhis suspect Punjabis will “steal” the waters of “their” Indus. They fear that new canals from the dam's reservoir will reduce the flow of water and leave the fertile Indus delta in Sindh vulnerable to the encroachments of the Arabian Sea.

In Sindh, even members of General Musharraf's own ruling coalition are afraid of openly supporting him. In early

January the Muttahida Qaumi Movement (MQM), which controls Karachi and the urban areas of Sindh, threatened to quit the Sindh government unless the Kalabagh project was ditched, and military action in Baluchistan halted. It took Pakistan's prime minister, Shaukat Aziz, and General Musharraf an hour each on the phone to placate Altaf Hussain, the MQM's leader, who lives in self-imposed exile in London.

This week, General Musharraf was forced into an embarrassing retreat. Instead of Kalabagh, he said on national television, two other dams would be built first. MQM workers celebrated by dancing on the streets of Karachi. Yet delay in building a string of big dams, including Kalabagh (the most feasible one), could seriously impair agricultural productivity and energy supplies. According to a World Bank study, Pakistan is already one of the most water-stressed countries in the world, “a situation which is going to degrade into outright water scarcity”. Pakistan has only 150 cubic metres (33,000 gallons) of water storage per person compared with over 5,000 cubic metres in America and Australia and 2,200 in China.

Many Pakistanis criticise General Musharraf for making his own life difficult by picking fights on so many controversial fronts. He seems rattled by the opposition he has provoked, and has resorted to bluster. In December he thundered against the rebellious Baluch tribesmen: “I will sort them out—they won't know what hit them.” In the event, the insurgents almost downed an army helicopter carrying the top military commander in Baluchistan. The rebels also had the audacity to lob rockets at General Musharraf himself when he visited the area last month.

If unchecked, the Baluch insurgency could destabilise the region and jeopardise oil and gas exploration, which are critical to Pakistan's economy. Similarly, any laxity in prosecuting the war against militants in the tribal areas bordering Afghanistan would hurt relations with America, Pakistan's most important benefactor. As it is, the Americans are still pressing for a chance to interrogate the disgraced scientist, Abdul Qadeer Khan, outside Pakistan about help he is alleged to have provided for Iran's nuclear programme. Handing the father of Pakistan's nuclear deterrent over would infuriate nationalists at home.

Besieged as he seems to be, General Musharraf still shows no inclination to broaden his political base by making friends with the parties of Benazir Bhutto and Nawaz Sharif, two exiled former prime ministers. Rather, he seems to see the presidential elections due next year as a chance to weaken them further, and consolidate his own power. Ruling Pakistan is not at all easy, even for an all-powerful dictator who, most observers reckon, sincerely wants to do well by the country.

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Economist.com WORLD ASIA

Kashmir

The long game

Jan 19th 2006 | DELHI
From The Economist print edition

A glimpse of a Kashmir settlement, if India wants one

Reuters

As good as it gets

THE latest series of five-day cricket matches between India and Pakistan began on January 13th with two days of aggressive Pakistani batting. When its turn came, India had no choice but to try to avoid defeat by batting out the match. The two countries' peace process seems to be running on similar lines. Adventurous Pakistani diplomacy tries to force a result: India plays for time.

On January 17th, the neighbours' most senior diplomats met in Delhi for the latest talks in a two-year old “composite dialogue”. The two sides have made great strides in establishing confidence-building measures, such as cricket matches. But there is little sign of real progress on the dispute that has soured their relations for nearly 60 years: divided Kashmir.

Pakistan's president, Pervez Musharraf, has often expressed frustration, and keeps coming up with ideas, which India sniffily rejects or ignores. Yet the general's latest musing, which, typically, was spelled out in a television interview earlier this month, is tantalisingly close to something India could, in theory, accept. India's prime minister, Manmohan Singh, insists that there can be no redrawing of international boundaries, ie, of the “line of control”, disputed by Pakistan, that divides Kashmir in the absence of an agreed border. General Musharraf's latest formulation accepts this. He argues instead for “self-governance” (which, he says cryptically, “falls in between autonomy and independence”) in both Indian- and Pakistani-controlled Kashmir and a period of “joint management” of some subjects by India, Pakistan and Kashmiris themselves.

India resents General Musharraf's habit of conducting his diplomacy through television interviews and refused to comment on this. But it does seem to contain at least a basis for negotiation, which in the past has been missing. The climate, however, does not seem conducive to a breakthrough. The general raised Indian hackles by suggesting again that India should “demilitarise” some of Kashmir, pointing out that “self-governance” will hardly be possible with hundreds of thousands of Indian soldiers there.

Indian patience was already strained by what it says is continued Pakistan-inspired terrorism in Kashmir itself as well as a co-ordinated bombing in Delhi last October, in which more than 60 people died, and a gun attack in a science institute in Bangalore in December. The general himself had been incensed by India's expression of concern about the “spiralling violence” in Baluchistan, and in turn accused India of financing and training insurgents, which India denies.

This exchange of accusations recalled the bad old days before the peace process was launched in 2003. But the talks in Delhi made some progress, with discussion of more confidence-building measures, such as the opening of new crossing-points on the line of control, and an Indian proposal to halt building of new army posts along it. A bus that sporadically links the capitals of the two parts of Kashmir remains the most visible sign of progress.

None of this, however, is likely to mollify Pakistani critics of the peace process, who suspect that India has no real interest in a Kashmir settlement, sees the peace process as an effective means of avoiding one, and strings the general along.

Nor can India point to much progress in efforts to repair relations between Delhi and Indian-held Kashmir. Mr Singh met the main separatist group, the All-Party Hurriyat Conference, last September, but there has been no

follow-up. On January 14th he met Sajjad Lone, a Kashmiri separatist leader who has fallen out with the Hurriyat. This was portrayed as part of an effort to engage all sides of Kashmiri opinion. That is a worthy aim. But it is taking a very long time, and many Kashmiris, as well as Pakistanis, are in a hurry.

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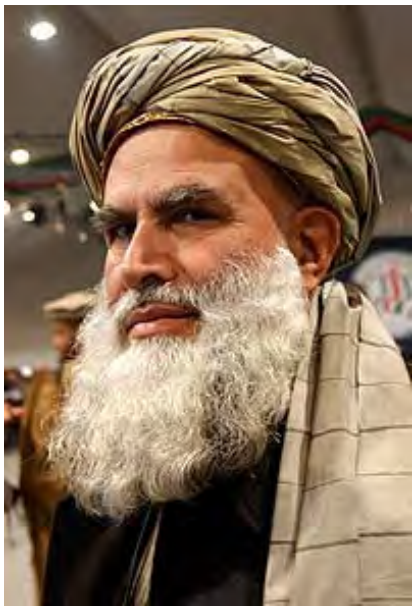
Afghanistan

Where's the justice?

Jan 19th 2006 | KABUL
From The Economist print edition

How to bring war criminals to book

Reuters



The near-respectable Sayyaf

ASSADULLAH SARWARY, who is accused of mass murder and torture, is the only person currently facing war-crimes charges in Afghanistan. His trial resumes this week. The secret-police chief under the Soviet-backed Tarakai regime of the late 1970s, he has been languishing in prison for 13 years and faces the death penalty if convicted.

It is an irony lost on few, least of all Mr Sarwary, that while he stands in the shadow of the gallows, a number of the leading personalities taking their seats in the new Afghan parliament have well-documented allegations of involvement in war crimes outstanding against them. A mechanism to bring past offenders to book, similar to those seen in Rwanda, Sierra Leone or East Timor, has been discussed but repeatedly deferred since the Taliban's overthrow in 2001. Stability, goes the argument, must come first. Now, with the election of Afghanistan's parliament completing the process of establishing democracy laid down in Bonn in 2001, stable government has theoretically arrived. But many of those who might face trial are an elected part of it.

Enthusiasm for pursuing war-crimes trials has, until recent weeks, been limited on the part of the outside world, too. However, ordinary Afghans appear to be eager for action. In January 2005, a survey of 6,000 Afghans by the Afghanistan Independent Human Rights Commission found that 90% wanted figures guilty of war crimes excluded from public office. Three times as many people wanted trials for major war criminals as wanted any lesser sanction such as compensation or a “truth and reconciliation commission”.

The prevailing sentiment within the government of President Hamid Karzai has been that raking over the past will do little but stir trouble and exacerbate old inter-ethnic tensions, derailing the drive for national unity. A contrary argument, however, is that failing to deal with the tainted figures still holding office, many with continuing ties to drugs and other criminal activity, will itself fuel disunity, encouraging private retribution and undermining the credibility of the government.

In early December, the Afghan cabinet approved a five-point plan for “transitional justice”, after considerable internal wrangling. It encompasses reform of the judicial system, vetting of officials and the use of traditional justice and conciliation mechanisms, as well as the potential for trials within three years. The plan has been welcomed, though it contains plenty of wriggle room if the government wishes to stop or slow the process.

If the Karzai administration seemed unlikely until recently to pursue the issue with vigour, the past weeks have seen a surge in interest from abroad. Ahead of next month's conference in London on future aid, some European governments are said to believe that aid must depend on reforms that would include some action on war crimes. Pressure from America also appears to have increased under its new ambassador, Ronald Neumann.

An additional spur has been the emergence of Abdul Rasul Sayyaf as one of the dominant forces in the new parliament. The crimes of his militia, particularly during the siege of Kabul in 1992, are some of the best-documented of Afghanistan's long war. Mr Sayyaf is also a radical Islamist with past links to Osama bin Laden. He missed becoming the parliament's speaker by only three votes. His case, above all, cries out for investigation.

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New Zealand

The last battle

Jan 19th 2006 | CLEVEDON AND KUROW
From The Economist print edition

Farmers are fighting for survival in the backdrop to Narnia

TRAFFIC halts along a southern highway with turquoise rivers and lakes. A horse has bolted from a Kurow farm, on New Zealand's South Island. A hiker must have let him out, the farmer's daughter fumes, as she chases the animal down. At the other end of the country, on a picturesque farm in Clevedon near the northern city of Auckland, Keith Kelly worries whether he can still afford to retire by selling off part of his large and hilly farm.

Such situations are increasingly common in New Zealand these days. The trouble started last June when the acting rural-affairs minister proposed creating a right of public access to a five-metre (16 feet) wide strip of land along all coastlines and waterways, on private land as well as public. Then last month the Auckland Regional Council made a bid to classify vast rural areas as “outstanding natural landscapes”. The goal, says Philip Pannett, the council's planning manager, is to protect 125,000 hectares (310,000 acres) around Auckland from development. This includes excellent coastal landscapes and volcanic cones, something the public wants protected, he adds. By heavily restricting the further subdivision of properties in this area, views should remain uncluttered by houses, fences and drives.

Mr Kelly, who heads the Auckland farmers' federation, sees the policy as a new violation of property rights and wants it scrapped, or the landowners compensated. He also fears the policy will eventually include provisions on access.

Land issues have become ever more pressing since New Zealand-based films including “The Lord of The Rings”, “King Kong” and “Narnia” started to attract record numbers of tourists to New Zealand and foreign purchases of its land. Camping grounds and open land are being rapidly converted into condominiums or posh estates, which makes public access to beautiful areas scarcer.

Many farmers feel they are being asked to shoulder the burden. Last June the National Board of Federated Farmers staged a week-long protest against the waterways proposal. By July the policy was being rethought. But the Auckland council policy has farmers threatening to protest again.

Farmers still fret about theft and damage to property and livestock. The horse at Kurow, for instance, had to be put down. They worry too about the safety of walkers, and about their property rights being salami-sliced away. Mr Kelly and his fellow-farmers understand the desire to protect beauty. The back view from his farm is stunning and includes the Haureki Gulf, Coromandel Peninsula and Auckland's harbour. “I can see why people want it,” he sighs. “But if you want it, then buy it or lease it.”

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China and Africa

No questions asked

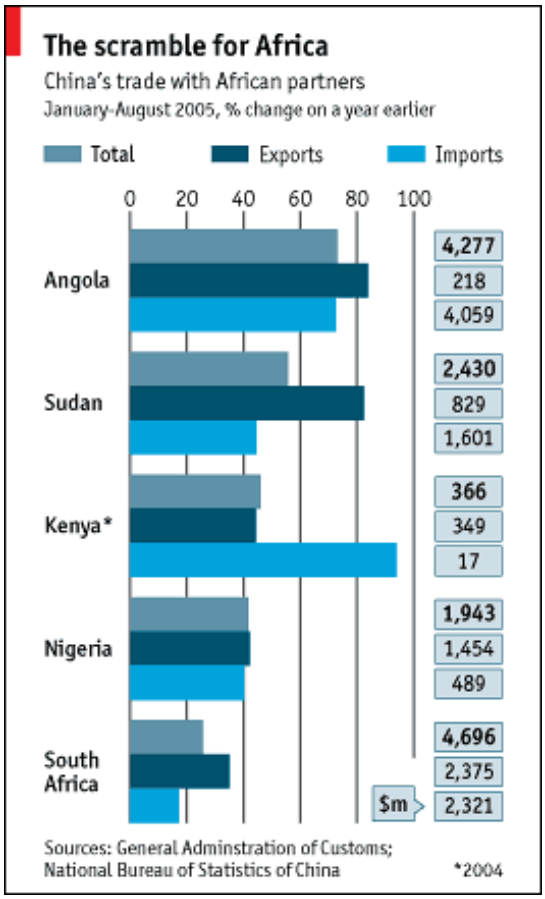
Jan 19th 2006 | BEIJING AND LAGOS
From The Economist print edition

Human rights are no bar to China's hunt for resources

CHINA has long been an advocate of keeping human rights and other pesky political issues separate from business, and in Africa it is practising what it preaches. In recent years, China has rapidly stepped up its involvement there, finding not only the resources it so urgently needs, but also willing business partners in places—Somalia, Sudan, Zimbabwe, Ethiopia and Libya, among others—where many western nations have been reluctant to do business at all. In 2004, the new Chinese president, Hu Jintao, made Africa one of his first foreign destinations.

China is hardly new to Africa. Nearly six centuries ago, Ming Dynasty seafarers reached the continent's eastern shores, and brought back a giraffe to satisfy the curiosity of their emperor. Today, Chinese vessels are regularly plying those same sea lanes, bringing back oil, iron ore and other commodities to satisfy the voracious appetite of a huge and growing economy.

Meanwhile, Chinese entrepreneurs are pouring investments worth billions of dollars into Africa. On January 9th, China's state-run energy firm, CNOOC, announced the purchase, for $2.27 billion, of a 45% stake in a Nigerian oilfield (see article). Apart from mines and oil, China has invested in resort hotels, agricultural and infrastructure projects, retail ventures and much else. China reckons its trade with Africa last year at nearly $40 billion (see chart), and rising fast. China now gets 30% of its oil from Africa, mainly from Sudan, Angola and Congo-Brazzaville.



Since Mr Hu's 2004 visit, China has secured oil from Gabon, an $800m deal to buy 30,000 barrels a day from Nigeria and a loan of $2 billion to Africa's second-biggest oil producer, Angola, for infrastructure development in return for oil. Chinese firms have tendered for contracts in telecoms and infrastructure across the continent. The strategy has been to widen trade and investment links while continuing the tradition of goodwill by boosting help for anti-AIDS programmes, education, culture and infrastructure—and in the case of Nigeria, launching satellites into space.

In its latest push, China this week sent its foreign minister, Li Zhaoxing, on a six-nation African visit, coinciding with the release on January 12th of a government white paper outlining its African policy. Amid the usual talk of mutual benefit and friendly co-operation, the paper called for greater Sino-African military co-operation, and said China would, “when conditions are ripe”, be willing to negotiate a free-trade agreement with the continent.

European governments are increasingly concerned at China's involvement, because it undermines their own efforts to tie trade and aid to human rights, and to help Africa overcome corruption. They fear that Chinese companies show scant regard for either consideration. In Ethiopia for instance, which has seen much of its European aid suspended because of gross human-rights abuses, China is believed to have offered to make good any shortfall. In Sudan, which has been accused of genocide, Chinese state firms have built a refinery and are getting involved in production. In repressive Equatorial Guinea, China is also sniffing out opportunities to rival the dominance of western companies.

The CNOOC deal in Nigeria has in particular raised eyebrows, partly because the company has bought a block that a rival energy consumer, India, had shunned after an initial bid. The stake was sold by a former Nigerian defence minister, who was awarded it when Nigeria was under military rule. That China has entered into this deal, when details of the ownership structure and contractual stipulations are so unclear, speaks volumes about the kind of risks it is willing to ride out in Africa to secure energy supplies.

While western governments may fret about China's growing influence in the region, some Chinese analysts see a measure of irony in the country's new role. Back in the 1960s and 1970s, China was more interested in world-wide revolution, third-world solidarity and the backing of African liberation movements. Now, according to one scholar at the Chinese Academy of Social Sciences, China's behaviour has more in common with that of the colonisers. “Since we are mainly there to make money and get hold of their resources,” he says, “it's hard to see the difference.”

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Taiwan

Desperate Chen

Jan 19th 2006 | TAIPEI
From The Economist print edition

An embattled president circles the wagons

AFP

Increasingly alone at the polls

Get article background

WHEN Yu Shyi-kun, a former prime minister, was elected chairman of Taiwan's Democratic Progressive Party on January 15th, many wondered why he wanted the job. The last two chairmen had to resign because of the party's repeated disappointments at the polls.

Mr Yu owed his ascendancy to a trouncing of his party in local elections in early December by the “pan-blue” alliance of the Kuomintang and the People First Party, which resulted in the resignation of his predecessor, Su Tseng-chang. Mr Su, however, has now become prime minister in his turn after the sudden “resignation” on January 17th of Frank Hsieh—the fourth prime minister since 2000. Like the party chairmanship, the job of prime minister does not amount to much in Taiwan, since executive power is held by the president, and the DPP lacks a majority in parliament. But the changes show that a deeply unpopular president is circling the wagons.

When President Chen Shui-bian was re-elected in March 2004 he appeared to have performed a miracle, turning a 20% opposition lead into a narrow victory. It has been downhill since then. First came the failure of his party and its allies to win a legislative majority in elections in December 2004. Many blame Mr Chen for campaigning on questions of national identity, not bread and butter issues. Following this, the government's inability to take a firm line on the pan-blue's dalliance with China—both parties' leaders visited Beijing last year—made Mr Chen look impotent. His popularity has slumped since then.

In the past Mr Chen has responded by banging the anti-China drum. He may be planning this again. His new year's speech suggested a tightening of economic policy toward China, though details have yet to be forthcoming. The conciliatory Mr Hsieh is believed to have disapproved of this policy; his replacement by the feisty Mr Su would give the president a premier more amenable to China-bashing, while Mr Yu, as the new DPP head, is an ultra-efficient Chen loyalist who will win over dissenters among the party faithful.

Even if this strategy restores Mr Chen's standing among his core supporters, it is unlikely to win the wider support it once did. China (Hong Kong included), buys nearly 40% percent of Taiwan's exports. The relationship across the strait is, to most Taiwanese, now far too important to disrupt.

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Palestine's election

Hamas ahoy!

Jan 19th 2006 | JERUSALEM
From The Economist print edition

The Palestinians' Islamist movement, Hamas, is set to do well in next week's parliamentary election. Will that hurt or help prospects for peace?

WITH less than a week to go, the reality has sunk in. Every attempt to contain Hamas has had the opposite effect. When Palestinians elect a parliament on January 25th, for the first time in a decade, they are expected to give the Islamist movement a good proportion of seats, in a resounding protest vote against the failures of the Palestinian Authority (PA) and its ruling Fatah party, and against Israel.

According to a poll published last week by Birzeit University, the “Change and Reform” party—the banner under which Hamas has fielded its candidates for the 132 seats in the legislative council—would get 30% of the national vote, against Fatah's 35%, the narrowest gap seen so far. That looks like the voters' answer to Fatah's infighting over candidacies, which produced a split in the party in December and ended in an untidy compromise between the warring factions: a list designed to soothe as many warring egos as possible instead of attracting as many voters as possible.

Moreover, the poll may underestimate Hamas's strength, since only half of the seats will be chosen by proportional representation. The other half will go in district elections, where Hamas has done a better job of choosing its candidates than Fatah, and where some disgruntled Fatah exiles are campaigning as independents, so splitting Fatah's vote. A previous poll put the two parties neck-and-neck in the district race. And even though Hamas is not expected to win more seats overall, Fatah's vote in the parliament could often be split, giving Hamas the advantage.

A lot of the blame can be put on the PA's president and Fatah leader, Mahmoud Abbas (Abu Mazen). He seems to have the right intentions, but his inability to control Fatah's chronic factionalism has undone him. The PA has failed to provide what opinion polls show matters most to Palestinians: domestic law and order. The Gaza strip, in particular, has been a mess of clan battles, kidnappings and score-settling since the Israelis vacated it in the summer. Some of the violence is suspected to be the work of senior Fatah leaders trying to weaken Mr Abbas or one another. And apart from making ordinary people feel unsafe, one indirect effect has been to hurt their pockets.

An “Agreement on Movement and Access” signed by Israel and the PA in November, which was supposed dramatically to ease the traffic of Palestinian workers and goods both within the occupied territories and across their borders, is already way behind schedule. Incidents like this month's violent takeover of Gaza's Rafah border

crossing by Palestinian police have given Israel reasons to delay lifting its restrictions. Thus, and despite a flood of promises of donor money for new projects, Gaza feels no less poor than it did before the Israelis left. Now it is harder to blame anyone but the PA, which, to top it all, is facing a fiscal crisis entirely of its own making.

What makes Hamas's appeal so great is that it does not just rest on its past performance—social programmes, leading the *intifada*'s violence against Israel, and a reputation for honesty—but on a canny, forward-looking campaign, starting with its new party name. It stresses domestic issues: education, welfare, law and order. The thornier questions of whether to continue its lull in attacks on Israel, declared last year, and what stance it might take on possible peace talks, are in the background. (Its manifesto makes no mention of Israel's destruction, which Hamas's charter calls for.) So is the question of whether and how it would impose Islamic law, such as bans on drinking, dancing and other forms of frivolity—a question that bothers most Palestinians, who prefer a secular state. When pressed on such questions, its candidates are evasive.

More and more Israeli commentators are also beginning to recognise that Israel's attempts to exclude Hamas—such as a mass arrest of its candidates, targeted killings of a few of its fighters, and a clumsy attempt to prevent or restrict voting in East Jerusalem because of Hamas's participation—have only added to the movement's credibility. Warnings from America and Europe that the PA might lose foreign funding if it includes Hamas, a listed terrorist organisation, have had a similar effect.

If the election is held—and it would be political suicide for Mr Abbas to ditch it now—a big unknown is how the results will be received. One worry is that Fatah fighters may sabotage or dispute the outcome, especially if Hamas looks like doing too well. A failure to get the result accepted would mark the final collapse of Mr Abbas's authority. And that will make it even harder for Israel's prime minister, whoever that is after its own election at the end of March, to decide how to deal with a PA that might contain Hamas ministers.

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Israel v Iran

Family feud

Jan 19th 2006
From The Economist print edition

Not so alien, after all

IRAN'S president, Mahmoud Ahmadinejad, says Israel is an alien implantation whose people should return to Europe or perhaps settle in Alaska. So it is an irony that Israel's president, Moshe Katzav, is in fact a Farsi-speaker born in Iran. Ditto Israel's defence minister, Shaul Mofaz, who is doubtless preoccupied nowadays with how to destroy Iran's nuclear programme. He is advised by Dan Halutz, Israel's former air-force commander and now chief of staff. Lieut-General Halutz was born in Israel, both his parents in Iran. They seem to have taught him a sense of humour. Asked how far Israel would go to stop Iran's nuclear programme, he replied: “two thousand kilometres”.

Getty Images

Halutz ponders a return visit

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Iran

All still to play for

Jan 19th 2006
From The Economist print edition

Pressure builds slowly, and Iran plays for time

AFP

Ahmadinejad ponders nuclear plans

IF IRAN'S nuclear ambitions are as peaceful as it claims, it is doing its best to disguise it. Faced with its determination to resume uranium enrichment (a skill also needed for bomb-making), Britain, France and Germany have called an emergency meeting of the 35-nation board of the UN's nuclear watchdog, the International Atomic Energy Agency (IAEA), for February 2nd. They hope to have Iran's past safeguards violations reported speedily to the UN Security Council.

By breaking the agency's seals last week on its pilot uranium-enrichment plant at Natanz, Iran has also alarmed Russia and China. Meanwhile, Israel's acting prime minister, Ehud Olmert, mindful of the desire of Iran's president, Mahmoud Ahmadinejad, to "wipe Israel off the map", this week said that "under no circumstances" could his country allow a hostile Iran to develop nuclear weapons. For the first time, Egypt and Saudi Arabia also called publicly on Iran to drop its nuclear defiance.

But would Russia and China let the Security Council put real pressure on Iran? Russia's president, Vladimir Putin, this week told Germany's chancellor, Angela Merkel, that while "abrupt and erroneous steps" (code for military action) must be avoided, Russia's position was "very close" to that of the Europeans. Russia was clearly angered that Iran brushed aside its own proposal to enrich uranium on Iran's behalf, to create space for more talks.

China is more hesitant. But European officials were pleased two weeks ago when it joined America, Britain, France and Russia (the other veto-wielders on the Security Council) in sending concerted messages to Iran, calling on it not to restart its enrichment activities. Such work had been suspended for more than two years to allow talks with the Europeans on a package of incentives that everyone had been hoping would encourage Iran to abandon its dangerous nuclear-fuel dabbling for good.

Mohamed ElBaradei, the IAEA's director-general, is also leaning harder on Iran. After three years' work detailing the gaps in its nuclear story, he has lately asked repeatedly for access to additional documents, people and sites. If Iran does not co-operate fully in time for a report to the next regular IAEA meeting, in March, his inability to confirm the peaceful nature of Iran's programme, he suggested in a recent interview with *Newsweek*, would "reverberate...around the world."

All it takes for a referral to the Security Council is a majority of the IAEA's board. But the Europeans want to gather as much support as possible. Hoping to try to avert such isolation, Iran this week claimed it was ready to resume negotiations with Europeans, and promised to study "seriously" Russia's enrichment proposal.

However, thinking has already started on what the Security Council might do to persuade Iran of the error of its ways. The first step would likely be a call for Iran to reinstate its enrichment suspension (it has not actually done any enriching yet) and co-operate fully with IAEA requests. If it still refuses, the Council could require it to do so. Even then, any sanctions would likely start small: travel bans for government leaders or those involved in nuclear work, a cut in sporting ties (maybe a ban from the soccer World Cup) and the like.

Agreement on economic sanctions would be much harder to achieve, as several countries, including Russia and China, but also Japan, India, South Korea and others, have important energy contracts with Iran, OPEC's second-biggest oil producer. Simply by talking of cutting its oil exports in retaliation, Iran this week helped talk up the market price of oil. A cut in supplies could send it far higher. Though that, said an American senator, John McCain, this week, might be a price worth paying to deal with the Iranian nuclear problem.

But pressure, even at the UN, will be slow to build. Sitting on their pile of cash from recent high oil prices, Iran's

leaders may calculate that they can afford to punish the world more easily than the world can punish them, at least for a time.

Israel also worries that time is on Iran's side. While others debate how long it might take for Iran to get a bomb (anything from three years to a decade), it frets that, once enrichment restarts, it will take Iran a year or less to learn to produce fissile material well enough to surmount the biggest obstacle to bomb-making. So far, everyone, including the Israelis, says they support diplomacy to contain Iran's nuclear ambitions. But that could change.

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Kuwait

Sheikh-up

Jan 19th 2006 | CAIRO
From The Economist print edition

Monarchs of the Gulf have been proving mortal

OIL prices may be sky-high, but this is not necessarily a great time for rulers in the Persian Gulf. Within a few short months, death has struck down four out of 12 reigning monarchs in a region that includes one sultanate, two kingdoms and nine emirates, seven of the latter being embraced within the United Arab Emirates.

The latest to pass away is Sheikh Jaber al-Sabah, who had ruled Kuwait since 1977. As with the earlier deaths of Sheikh Zayed of Abu Dhabi, King Fahd of Saudi Arabia and Sheikh Maktoum of Dubai, the succession appeared smooth enough. Yet Kuwait's case highlights some of the problems inherent in any system of inherited power. Monarchy in the Gulf is complicated further by arcane rules and huge families.

The crown prince who has taken over as emir, Sheikh Saad al-Sabah, is so decrepit that there are fears he may not be able to read the brief oath before parliament that Kuwait's 1962 constitution requires him to take. By custom, Kuwait's leadership does not pass from father to son, or even from elder to younger brothers as in other Muslim dynasties. It alternates between two branches of the al-Sabah family, known as the al-Salem and al-Jaber lines, after the two sons of the current ruler's great-grandfather, Sheikh Mubarak, who died in 1915.

That has worked well, but suspicions have lately grown that the al-Jabers have been quietly elbowing out their al-Salem rivals. Kuwaitis note, for example, that the current 16-minister cabinet includes just one al-Salem, but no fewer than six al-Jabers. The more cynical believe that the powerful prime minister, Sheikh Sabah al-Sabah, wishes to become emir himself, and so was pleased to see his half-brother, Sheikh Jaber, replaced by a feeble al-Salem, who fulfils the alternation rule but may not stay in office very long. In recent months some al-Salems have quietly protested against what they see as a looming usurpation of their rights. MPs have also demanded a bigger say in the matter.

Yet though such jockeying arouses passions, even in relatively democratic Kuwait it remains mostly a spectator sport. As in other Gulf states, it may take more than a family squabble to shake the complacency of Kuwait's 950,000 citizens. Last year the emirate, which owns a tenth of the world's known oil reserves, earned itself a tidy $45 billion in revenues.

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Nigeria

Pouring trouble on oily waters

Jan 19th 2006 | LAGOS
From The Economist print edition

AP

Go tell your shareholders

Rebels in the main oil region are threatening stability nationwide

TROUBLE in the Niger Delta, Nigeria's turbulent oil-producing region, is getting worse. Last week, after a major pipeline feeding an export terminal had been blown up, boatloads of militants kidnapped four foreign oilmen, including an American and a Briton, from an offshore field belonging to Shell. The company had to cut daily output by 226,000 barrels, about a tenth of Nigeria's total output.

Four days later, rebels stormed a flow station in the same area, shooting dead at least four soldiers guarding the platform. Nigeria's army said it killed eight rebels. It was the fourth big attack on Shell, Nigeria's largest oil producer, since December. The disruption has rattled industry officials. Worse, they fear, may be to come.

Kidnappings and attacks on oil installations have been frequent in the delta, where armed militias roam the creeks, illegally tapping crude oil and building up their arsenals with the proceeds. Locals feel bitter towards the multinational companies because their villages remain dirt-poor; Nigeria's oil wealth passes them by. The ensuing resentment turns into anger.

The oil companies usually pay up fast to get hostages freed. But this time the Movement for the Emancipation of the Niger Delta (MEND), a previously unheard-of group claiming responsibility for the latest attacks, is upping the ante. It says it has “no desire or interest in abducting for ransom”: it wants to stop all exports. Foreign workers, it says, should leave the delta or die.

MEND has told Shell to pay $1.5 billion to one of the delta states, Bayelsa, for the pollution it says Shell has caused. The group also wants locals to control the delta's oil wealth and calls for the release of Diepreye Alamieyeseigha, a former governor of Bayelsa, who made similar demands before his arrest for alleged money-laundering. And MEND champions Mujahid Dokubo-Asari, a delta militant who laid down arms in 2004 but was later arrested on treason charges. These two men were not allies, but they have both become icons for the delta's biggest tribe, the Ijaw, many of whom say they get scant benefit from Nigeria's oil while having to live in a quagmire of oil slicks and gas flares.

Neither man is an angel. Mr Dokubo-Asari was an ally of another delta state governor who is widely thought to have rigged elections in his state in 2003. And Mr Alamieyeseigha, whose state gets one of the biggest allocations

of revenue because of its high oil production, did little for his people, lording it in a palatial house and yacht. A savvy member of a faction of Nigeria's ruling party, Mr Alamieyeseigha is clearly vying for influence ahead of next year's national elections.

In any event, tension and manoeuvrings in the delta affect national politics. Nigeria's president, Olusegun Obasanjo, is due to step down next year after two terms in office. An Ijaw rebellion in the western delta in the run-up to the last presidential race, in 2003, meant that about 40% of Nigeria's oil production had to be shut down. Since a 15-year-long stint of military rule ended in 1999, Mr Obasanjo has struggled, largely in vain, to bring benefits to ordinary Nigerians. Corruption and political thuggery are still messing things up.

MEND looks more sophisticated and may become more of a menace than previous rebel groups; its attacks in the delta are more co-ordinated. “This is a compact, well-trained group,” says Dimieari von Kemedi, an expert on security and politics in the delta, “but one that may have the capacity to grow as things unravel.” A senior Shell security official has said that Nigeria is losing control of the delta.

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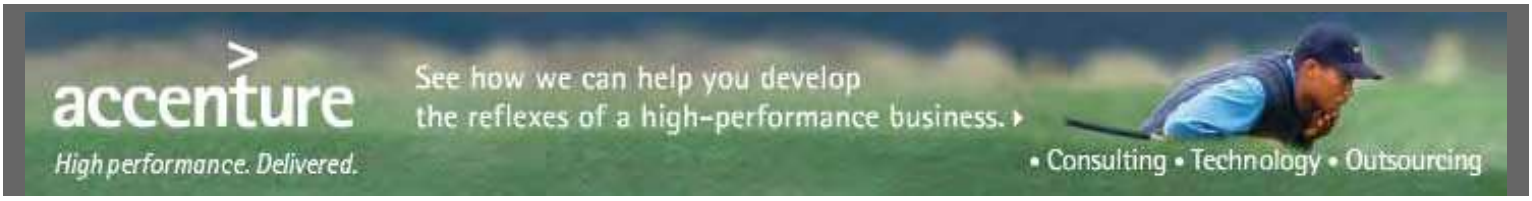
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Russia and the West

A colder coming we have of it

Jan 19th 2006 | MOSCOW
From The Economist print edition

AFP

Vladimir Putin may prove mildly constructive over Iran, but as Russia assumes the G8 presidency, he is not the partner the West once hoped for

Get article background

A POSSIBLY apocryphal story has it that, in the 1980s, Soviet troops in East Germany had to attend sessions of political instruction. Insubordinate air-force officers would skip the indoctrination and congregate at the buffet, where an ingratiating KGB man would try to wheedle them back in. The officers called him the “head of the club”. His name was Vladimir Putin.

Twenty-odd years later, the KGB-man-turned-president is head of another club: the G8 group of rich countries, whose presidency Russia assumed at the start of the year. Not so long ago, the idea of Mr Putin presiding over a gathering of free-market democracies might have seemed optimistic, but not altogether implausible. Yet, even before the gas-to-Ukraine squabble that marked the start of the year, Russia's membership of the G8 was looking hard to reconcile with its trajectory under Mr Putin. Russia's relationship with the West has changed, incrementally but surely, for the worse. Why?

The true transformation may have taken place not inside the Kremlin but in foreign perceptions. Like Russian voters, foreign leaders were at first beguiled by Mr Putin's difference from his predecessor, the erratic and unpredictable Boris Yeltsin. Mr Putin was sober, business-like, apparently reliable and impressively committed to macroeconomic stability.

Andrei Illarionov, a maverick liberal economic adviser to Mr Putin who finally resigned in December, bewailing a decline in political and economic freedom, identifies the start of the Yukos affair in July 2003 as a key turning-point. But in fact the tendencies that have been causing international concern to mount during Mr Putin's second presidential term were evident throughout his first, in 2000-04: harassment of uppity tycoons, centralisation of political power and suppression of an independent media, not to mention the brutal war in Chechnya.

In the rose-tinted years, some western diplomats mistook what now looks like a tactical decision—Mr Putin's embrace of the United States after September 11th—for a strategic one. As circumstances changed over the years, old KGB instincts returned to the fore. In foreign-policy terms, that has meant a zero-sum attitude to diplomacy;

the pursuit of great-power status, especially via energy exports; and a propensity to believe that the rest of the world thinks and acts in just the same way. Russian interference in the Ukrainian elections of last winter suggested that Mr Putin sees the democratic process merely as a way of legitimising power, not as an end in itself; it also disillusioned westerners who still hoped that revanchist domestic policies could be separated from foreign policy.

None of which means that Russia and the West can never work together. Indeed, they are trying to do so over Iran. Russia's commercial interests in Iran's civilian nuclear programme notwithstanding, the Kremlin's attitude to Tehran, says Rose Gottemoeller, a non-proliferation analyst at the Carnegie Moscow Centre, is “changing fast”. Apart from anything else, as more countries get the bomb, Russia's own cherished nuclear status becomes less valuable. Sergei Lavrov, Russia's foreign minister, this week emphasised the primacy of the non-proliferation regime, and the moratorium on Iranian uranium enrichment. Mr Putin revived the offer of a joint Russian-Iranian enrichment programme on Russian territory; the Iranians said they were considering it.

But there are differences of interest, even over Iran. For the Russians, the crisis represents an opportunity. As Bobo Lo, of the Royal Institute of International Affairs in London, puts it, Russia has a taste for “controlled tension”: diplomatic situations short of conflict, in which Russia's membership of the UN Security Council gives it extra clout, as in the run-up to the Iraq war. That influence is diluted if the Russians merely go along with the Americans and Europeans, or if the tension dissipates quickly. Such considerations may explain why Mr Lavrov argues that imposing sanctions on Iran is “in no way the best, or the only, way to solve the problem.”

The new-year gas row is unlikely to be the only source of friction between Russia and its G8 partners in the months before their July summit in St Petersburg. There will be parliamentary elections in Ukraine in March: although it increasingly looks as much a corruption scandal as a political spat, the gas dispute has contradicted the idea that the Kremlin has “accepted defeat” in Ukraine. Also in March there is a presidential poll in nastily authoritarian Belarus, where western advocacy of free elections will once again be interpreted in Moscow as impudent meddling in Russia's “near abroad”.

The pattern of western responses to Mr Putin now seems set: intermittent, mild public rebukes (such as the scolding by Condoleezza Rice, America's secretary of state, over the gas affair) balanced by conciliatory photo opportunities. To students of diplomatese, the public mentions by Angela Merkel, the new German chancellor, of Chechnya and the government's restrictions on non-governmental organisations, during her visit to Moscow this week, hinted at a welcome stiffening of Germany's approach.

Yet despite pressure from some American congressmen, there is little appetite to embarrass Mr Putin in St Petersburg. Mr Illarionov argues that, by attending the summit, the seven other world leaders will be seen as giving their “stamp of approval” to Russia's recent behaviour (though he glumly admits that there is not much they could do to change it). “That is not the impression we want to leave,” says one American official, arguing that to isolate Russia would only make things worse.

Further ahead loom Russia's own parliamentary and presidential elections, in late 2007 and early 2008. “Elections in a non-free country, as Russia is today, don't matter much,” sniffs Mr Illarionov. In foreign-policy terms, he may be right: the successor chosen by Mr Putin is likely to offer the same combination of prickliness and occasional pragmatism. (His nearest rival may be a strident nationalist, just the sort of bogeyman Mr Yeltsin used to conjure up to persuade voters and foreign interests to stay behind him.)

One leading contender for the top job is Sergei Ivanov, now defence minister and deputy prime minister, and another Russian politician who looks more western than he is. In a recent article in the *Wall Street Journal*, Mr Ivanov noted the emergence of new threats to national security that might require military action. “Chief among them,” wrote this ex-KGB man, “is interference in Russia's internal affairs by foreign states.”

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Germany's foreign minister

Schrödermeier

Jan 19th 2006 | BERLIN
From The Economist print edition

A foreign minister under pressure to account for the past

AFP

Steinmeier's stony silence

SOMETIMES a rising star can quickly become a fall guy. Consider Frank-Walter Steinmeier, Germany's new foreign minister. Since it emerged that two German spies in Baghdad had helped the Americans to avoid collateral damage or even to pick bombing targets during the Iraq war, critics have been calling for him to resign. Leaders of his own Social Democratic Party have deemed it necessary to assure him of their support.

Mr Steinmeier has amply lived up to his reputation, earned as chief of staff to Chancellor Gerhard Schröder, for competence, efficiency and loyalty. He is as voracious a reader of briefs in the foreign ministry as he was in the federal chancellery. He managed to extract German hostages from Iraq and Yemen. And he allows Angela Merkel, his Christian Democrat boss, to set the pace in foreign policy.

Yet Mr Steinmeier has one big weakness: his past as Mr Schröder's grey eminence. Whenever something unpleasant related to Mr Schröder's chancellorship emerges, it falls straight into Mr Steinmeier's lap. In December, it was CIA shenanigans—the renditions of terrorist suspects via German airports, the kidnapping of Khaled al-Masri, a German citizen. Now the issue is exactly what information was passed to the Americans during the Iraq war.

Under Mr Schröder, Mr Steinmeier was responsible for co-ordinating Germany's intelligence services. He has confirmed that the federal intelligence service kept two agents in Baghdad who helped the Americans with co-ordinates for “non-targets” such as hospitals and embassies. But press reports suggest that more sensitive military information was passed on. Critics are arguing that Mr Schröder lied when he promised that Germany would not join the war.

Before and during the Iraq war, Mr Schröder faced a tricky balancing act. He had to come out against the invasion—but he had no interest in further upsetting Washington. Thus, he did what he could to help without losing credibility: allowing American military planes to fly over German territory, getting German soldiers to protect American military installations—and exchanging intelligence.

Could two agents be enough to turn Germany into a member of the “coalition of the willing”? Mr Steinmeier has said that “alleged witnesses in dark rooms” should not be allowed to “rewrite history”. Another question is why the story was leaked now. If the source was the Pentagon, as many in Berlin believe, it may be that the motive was revenge on Mr Schröder. Or perhaps the hard-pressed CIA wanted to show that the Europeans are not clean, either.

Mr Steinmeier may survive for a while, even though the opposition is demanding a parliamentary inquiry. He will surely have tried to keep his erstwhile boss (and himself) out of trouble. But he has conceded that “yes, they do exist, the less glitzy sides of power beyond media events and talk shows.”

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France and the European Union

Desperately seeking a policy

Jan 19th 2006 | PARIS
From The Economist print edition

France no longer knows where it wants the European Union to go

SIX years ago, Joschka Fischer, Germany's foreign minister, gave a landmark speech on Europe at Berlin's Humboldt University. There was thus a certain symbolism in the decision by Dominique de Villepin, France's prime minister, to choose the same place for his first big speech on Europe, on January 18th. Compared with Mr Fischer, Mr de Villepin was short on institutional ambition. But that is not surprising: eight months after French voters rejected the European Union constitution, France is in disarray over Europe.

Mr de Villepin called for a revival of the Franco-German motor to get European integration moving again, in a way that responded to its citizens' fears. “France did not say no to Europe,” he declared. “She said no to a Europe whose purpose she no longer understood.” But on firm constitutional proposals he stayed mum.

Most French ideas on Europe nowadays touch on social and economic policy instead. President Jacques Chirac has called for “a Europe at once more competitive and more social”. The French have proposed a common European energy policy, and more spending on research and innovation. Catherine Colonna, France's Europe minister, argued this week for a European civilian service and more student exchanges. Mr de Villepin suggested a Franco-German border police.

In one sense, this emphasis on things non-constitutional is natural. Europe is still in its “period of reflection”, agreed by all EU leaders after the French and Dutch voted no last summer. Until nearer the June EU summit, at the end of the current Austrian presidency, nobody is putting concrete institutional suggestions on the table. French ideas are particularly delicate. “There's little chance that any French proposal will get support in Europe right now,” argues Sylvie Goulard, a European specialist at Sciences Po, a university.

Yet the lack of a clear line also reflects something else: internal confusion about what France really wants. Valéry Giscard d'Estaing, the former French president who chaired the convention that drafted the EU constitution, puts it trenchantly: “For the first time in 50 years, France no longer has a project for Europe.”

This policy muddle has been on full display in recent weeks. Despite promising “ambitious proposals”, Mr Chirac has so far stuck to vague declarations, including a renewed call for his old favourite, “pioneer groups” of those willing to integrate faster. Both he and his prime minister want a debate on enlargement, but whereas Mr Chirac favours Turkish entry, Mr de Villepin is far cooler. This week he said that “the purpose of the union today is not to spread out indefinitely.” When Nicolas Sarkozy, interior minister and head of the ruling UMP party, declared last week that all future enlargements beyond Bulgaria and Romania should be suspended pending constitutional reform, the foreign ministry hastily stated that these were not the views of the French government.

The only area where there is agreement is one that dares not speak its name: a refusal to consider a second referendum or some other way of reviving the rejected constitution. Despite other countries' reluctance to renounce the text, the idea of consulting the French electorate again is considered absurd in Paris. Mr Chirac, whose popularity ratings have collapsed, knows he is in no position to persuade the French to have second thoughts.

France's difficulty is not just that its people are in a sour, rejectionist mood. It is also a pre-election year. The two keenest rivals on the right, Mr Sarkozy and Mr de Villepin, are engaged in a battle of attrition that guarantees recurrent disagreement, on Europe and much else. As for an enfeebled Mr Chirac, undermined by the French no, he is scarcely in a position to drive any European thinking. As the left-leaning *Libération* newspaper commented recently, “it's a bit like a pyromaniac offering his services to firemen.”

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Italy's prime minister and the law

Final fruits of office?

Jan 19th 2006 | ROME
From The Economist print edition

AP

Berlusconi seeks salvation

Parliament once again helps Silvio Berlusconi out of his legal troubles

SILVIO BERLUSCONI, Italy's prime minister, is ending his current term of office as he began it in the summer of 2001: with an assault on the judicial system. In one of its last acts before the election in April, the Italian parliament has passed a bill sponsored by Gaetano Pecorella, Mr Berlusconi's lawyer, who is also a deputy for his political party, Forza Italia. In July 2001 Mr Pecorella, who chairs the lower house's justice committee, also sponsored a law to downgrade the crime of false accounting, for which the prime minister was then on trial. That law shortened the statute of limitations after which charges are time-barred, a provision that directly benefited Mr Berlusconi.

The new bill would abolish the prosecution's right to appeal against acquittals by the court of first instance. By chance, a court in Milan is due to begin hearing just such an appeal, of a case in which Mr Berlusconi was acquitted on four charges of bribing judges. On one charge, the acquittal came because the crime was time-barred after extenuating circumstances had been granted; on two others, it came for lack of sufficient proof; on the fourth, it was because he had not committed the offence. But the prosecution appealed against all these verdicts, which were delivered in December 2004.

Cesare Previti, a Forza Italia senator and business colleague of Mr Berlusconi, might also benefit from the new bill. He has been found guilty in two cases of judicial corruption and faces a prison sentence should the verdicts be upheld. One of the cases, involving a company owned by Mr Berlusconi, was due to be decided by the supreme court this week, but the hearing was cancelled because of a lawyers' strike. Under the new bill, Mr Previti might be able to submit direct evidence to the supreme court, whose role is currently limited to ruling on points of law.

Magistrates are appalled by the new bill. “Its impact will be devastating,” comments Armando Spataro, a senior anti-terrorism prosecutor in Milan and a leader of the national magistrates' association. The bill could trigger a huge increase in the supreme court's workload, as defendants playing for time and hoping to benefit from the statute of limitations ask for the evidence to be reviewed yet again.

Constitutional lawyers have suggested two reasons why Italy's president, Carlo Azeglio Ciampi, may refuse to sign the new bill, however. They say that it runs contrary to the requirements that there should be equality between parties in trials and that trials should be of a reasonable duration. If Mr Ciampi sends the bill back to parliament, there may not be enough time left for it to be resubmitted before April's election.

By coincidence, Mr Berlusconi went to see investigating magistrates in Rome on the same day that parliament approved Mr Pecorella's law. Yet this did not herald a new, more cordial relationship with the magistracy. Rather, the prime minister claimed to have information relating to the role of opposition leaders in a bank takeover that

the magistrates were investigating. He later admitted that what he knew had no judicial relevance. Far from giving the magistrates a hand, the prime minister was, it seems, merely electioneering.

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Kosovo's future

Independent thinking

Jan 19th 2006
From The Economist print edition

The behind-the-scenes diplomacy that will settle Kosovo's future

IF YOU were to assess the future of Kosovo only from the local media, you might think that megaphone diplomacy was all that was happening. Kosovo will be Serbian forever, trumpet Serbia's leaders. The province's Albanian majority retort that nothing less than full independence will do for Kosovo's 2m people, more than 90% of whom are ethnic Albanians. It seems an impasse.

Yet behind the megaphones, tough negotiation has already taken place—albeit not between Serbs and Albanians. Since the end of the Kosovo war in 1999, Serbia's southern province has been under the jurisdiction of the UN, which last November appointed Martti Ahtisaari, a former Finnish president, to start talks on Kosovo's future status. The Serbs and Kosovo Albanians have assembled negotiating teams that are due to meet for the first time next week in Vienna.

But much of the hard bargaining has already happened, among interested outside powers: Britain, France, America and Russia. Given these countries' foreign-policy differences, the degree of consensus on Kosovo is surprising. Even Russian diplomats, who insist publicly that they will back the Serbs, say the opposite in private. The four powers all agree that Kosovo should have “conditional independence”, code for full independence after a transitional period, but with certain safeguards for Kosovo's remaining Serbs.

The only dispute is over tactics. At present, all are pretending that the future of Kosovo is to be settled in Mr Ahtisaari's talks. But in private it is accepted that, since the two sides will never agree, the decisions will have to be taken for them. British diplomats argue that the sooner an explicit guarantee is given to the Kosovo Albanians that independence in some form is coming, the greater the concessions they will be ready to make to Kosovo's 100,000-odd remaining Serbs. The French are more cautious, fearing that going public too soon may mean that the Serbs refuse to engage in any talks at all.

If the outcome is already agreed, what is the point of Mr Ahtisaari's negotiations? The answer, in the words of one diplomat, is that they “are not about the status of Kosovo...[but about] negotiating the status of the Serbs in Kosovo.” The Serbian government may still insist that Kosovo belongs to Serbia under international law, but such a position needs outside backing if it is to be credible. Realising that Russia's support is uncertain, the Serbs appealed last month to France. The French replied that they would support Serbia's legitimate interests, but only if they were realistic—and keeping Kosovo was not that.

A disappointed Boris Tadic, Serbia's president, is now preparing a fallback position. If Kosovo's independence cannot be prevented, he is putting out feelers to see if Serbia can, at least, stop the Kosovo Albanians having their own army and, for the foreseeable future, a separate seat at the UN. The Serbs give warning that, if Kosovo is lost completely, radical nationalists may come to power. A recent poll showed support for the nationalists holding up better than for other parties.

Yet this threat may not be that worrying, either. What would happen if the nationalists were to take control? Not much, shrugs one diplomat. Serbia's choice is, he says, “Belarus or Brussels”—isolation or Europe. As with Hobson's choice, it is really no choice at all.

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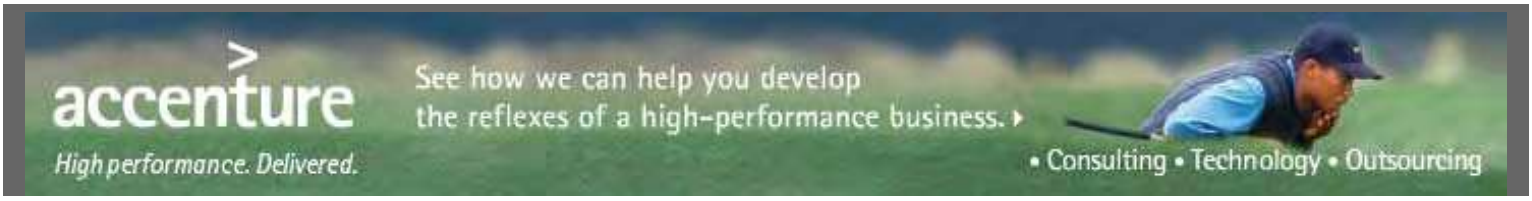
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Smoking in Spain

In your eyes

Jan 19th 2006 | MADRID
From The Economist print edition

A ban that may not have much effect

AP

Café debate, Spanish-style

AT THE start of the year, Spain became the latest European country to ban smoking in many public places. Its red-eyed, gravel-voiced smokers are incensed. Sergi Arola, the (non-smoking) owner of Madrid's La Broche restaurant, has enforced the ban, but not without rancour. “Why are they attacking public consumption? I only hope that one day a vegetarian minister is not going to ban steaks. With this measure we are heading towards ending the drink and the *tertulia* (café debates). To have an armagnac without a cigar is unthinkable.”

The Socialist government of José Luis Rodríguez Zapatero decided on a ban because smoking is the biggest killer in Spain, with 50,000 deaths a year. Some 30% of Spaniards smoke; Spain is the European Union's second-biggest consumer of tobacco per head. Smoking is now banned in offices, shops, schools, hospitals, public transport and theatres. Owners of bars and restaurants bigger than 100 square metres (1,000 square feet) have eight months to install separate smoking areas with ventilation systems. Smaller places must put up signs saying whether they are smoke-free.

The country's notoriously smoke-clad civil servants have had their ashtrays withdrawn. Bilbao town hall is distributing 20,000 ashtrays in an attempt to stop workers from chucking their butts in the street.

Similar bans have been imposed in Ireland, Italy and Norway. Britain plans to ban smoking in pubs and restaurants from 2007, with an exemption only for pubs that do not serve food. But compared with other European countries, the Spanish law is quite liberal—and it may prove to have little effect.

A government-sponsored opinion poll in November showed that more than 77% of respondents backed the ban. But 69% think it will be hard to enforce. Why? Most Spaniards answer that whoever makes the law, makes a loophole. The Spanish hotel federation points out that 90% of small bars have opted to continue to allow customers to smoke. There is also much dispute over what exactly constitutes a workplace. The health ministry has been inundated with calls from people wanting to know where they can light up. In Valencia a cafeteria located inside a government building reversed its initial ban after its habitual customers deserted it. In short, little may change for the determined smoker—and most Spanish bars will stay full of stale cigarette smoke.

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Charlemagne

Playing soft or hard cop

Jan 19th 2006
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Iran provides a test of both Europe's "soft power" and its relationship with hard power

NOT since Athens and Persia went to war in the 5th century BC has Iran mattered so much to Europe. For the past few years, it has been the biggest test of the European Union's ability to affect such global issues as nuclear proliferation and energy security. It is also testing whether that most characteristic EU foreign-policy instrument, soft power, can work beyond the immediate neighbourhood. To its supporters, soft power is a slower, surer, more civilised way of exercising influence than crude force. Does the evidence from Iran bear this out?

It should be conceded right away that Iran has given soft power a reasonably fair hearing. Although some Europeans complain almost routinely that American indifference has sabotaged their efforts, for most of the past year George Bush's administration has put its weight behind the British, French and Germans (the so-called European three) on Iran. Moreover, Iran itself signed up to the process, at least at the start.

Soft power has also had some successes. It may have slowed Iran's plans by a couple of years, delaying the confrontation over Iran's nuclear programme to 2006 rather than 2003, a time when many European countries were locking horns with America over the invasion of Iraq. Europe's attempts to help on Iran have soothed some of the transatlantic wounds left by Iraq, which in its turn helped to rally the Americans behind the European three. That could not have been predicted in 2003, when some members of the Bush administration were wondering whether Tehran should be the next stop after Baghdad.

Because the European three also spoke, in broad terms, for the union as a whole, they probably brought something to the talks that America could not have done on its own. Iran can hardly claim to be the victim of some American hegemonic plot, still less of Washington's fabled Jewish lobby, for instance. And the Europeans do seem to have been negotiating in good faith. This has made it sound more convincing to the rest of the world when they back the International Atomic Energy Agency's conclusion that Iran has been hiding parts of its nuclear programme and most governments' suspicions that Iran has been lying about its intentions.

As a result, it may be easier to isolate Iran than it would have been had no talks been held. And it has slightly increased the chance that Russia and China will be ready to back some sort of coercive action by the United Nations Security Council. Even if European diplomacy has now ended, it has put international institutions—the

IAEA, the UN—at centre stage for the next phase (see article). To Europeans, this is a good thing in itself.

What all this adds up to, however, is the conclusion that soft power may have been effective at changing the behaviour of America, and possibly Russia and China. That is, it sustained itself as a policy and was not undermined by western squabbles. Yet the original purpose was, presumably, to change the behaviour of Iran, by drawing it into a gentle web of mutual rights and obligations. Is Iran changing? Nobody outside Iran knows. Diplomatic efforts are continuing. But the signs do not exactly look promising. “Thank God, our enemies are idiots,” said one prominent Iranian cleric recently. Instead of thinking about a web of obligations, the Iranians are talking solely about their rights to have whatever nuclear technology they choose.

For soft power to succeed, both sides must want something from the other, and must be reasonably honest about it. Yet between 2003 and 2005—that is, even before the election of President Mahmoud Ahmadinejad—Iran was negotiating in bad faith. During this period, European officials believe, it continued to work in secret on nuclear research, having promised to suspend uranium enrichment.

Moreover, there is one issue on which soft power has nothing to offer. If Iran wanted a security guarantee (as some have suggested), then Europe, which has no significant military forces in the region and no power to affect regional stability, was in no position to provide one. Only America could do that. This does not mean the attempt to use soft power was a waste of time. But it suggests that European efforts would never have worked on their own. There always had to be a hard-power component, perhaps an Iran-America deal on security to match an Iran-Europe one on trade and proliferation.

Mars and Venus

For Europeans, that raises the toughest question of all. Does soft power support or supplant hard power? America backed the Europeans not just because it had no better idea what to do but because it thought European diplomacy might reinforce American bellicosity (and vice versa). To the Americans, there is merit in a good cop/bad cop approach to policing the world. Now that the good cop has suffered a setback, people are weighing their truncheons. John McCain, a Republican senator, has said that, bad as war would be, a nuclear-armed Iran would be worse.

But for true believers in soft power, the point is not to support but to supplant brute force. It is a better way of managing global tensions: a rival star, not a best supporting actor. To those who think like this, the talking can never stop. Some Europeans still say that military action is inconceivable and threats of sanctions are unhelpful. This seems a characteristic European cast of mind. Nothing is ever decided. The European project is never finished. And even if something seems to have been tried and failed, there is always a chance to try—and fail?—again.

The crisis with Iran has exposed rather than reconciled these transatlantic differences. They are likely to get sharper over the next few months. As Robert Kagan of the Carnegie Endowment argues, both hard and soft power have their characteristic flaws. Hard-power advocates can be too quick to pull the trigger—as, arguably, in Iraq. But for soft-power believers, there is never a trigger to pull—as, possibly, in Iran.

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Sex abusers and schools

The end of innocence

Jan 19th 2006
From The Economist print edition

Convicted child abusers are much less dangerous than the British public—and the government—believe

IN 2003, Paul Reeve was found to have done something illegal. Although he was not convicted of any crime, he accepted a caution from the police. He was banned from certain jobs. Then a government department reviewed Mr Reeve's case and lifted the ban. He took a job in Norwich, but quickly resigned after the police objected. It may not sound like the sort of scandal that would keep the media busy for a week and threaten the career of a government minister. But since Mr Reeve's crime involved child pornography, and his job was teaching physical education in a school, the level of panic—and the potential fallout—is almost without limit.

Memories of an earlier enormity are one reason for the hysteria. In 2002, two Cambridgeshire girls were murdered by Ian Huntley, a school caretaker. The crime was egregious enough, but it turned out that Mr Huntley had previously been investigated for rape, underage sex, indecent assault and burglary. A public inquiry revealed police incompetence and sloppy record-keeping. Such a person, it was promised, would never again be allowed to work in a school.

As the case of Mr Reeve demonstrates, though, a man who has been tarred with the brush of paedophilia is not prevented from working with children forever. A hurried review by the education department found 56 cases where child sex offenders were cleared to teach. One involved Keith Hudson, a science teacher who was convicted of possessing indecent images of boys. Mr Hudson was placed on List 99, which bars dubious characters from teaching jobs. But the education department allowed him to work in girls' schools.

Ruth Kelly, the much-barracked education secretary (see article), now says ministers should no longer decide such cases. She also promises to simplify the vetting system by creating a single, all-encompassing list. At present, there are no fewer than seven ways of checking someone's credentials.

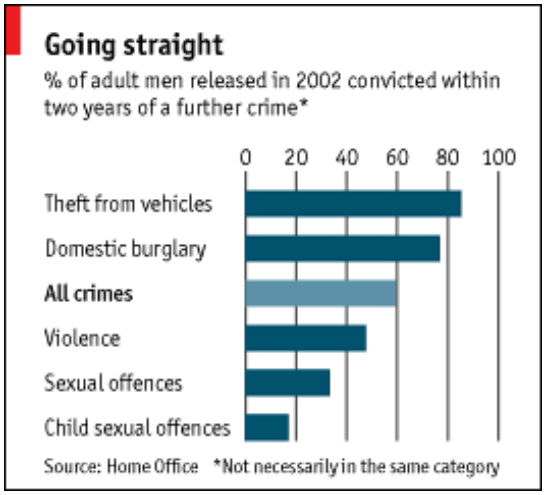
The British authorities place a good deal of faith in the power of lists to protect children. They have been inspired by America, where information about more than half a million sex offenders is available not just to the police but also to the public. Britain has not yet reached the point of barring sex offenders from living near schools or (as in Florida) from taking refuge in hurricane shelters. But it is easier to get on to a British list. A caution or, in some cases, the mere suspicion of child abuse may be enough.

Advocates of keeping lists and restricting employment point out that the sexual abuse of children is a horrendous crime which can lead to a lifetime of anguish. But the main justification is not the awfulness of the offence but the supposedly incorrigible character of the offender. “The nature of sexual attraction to children is that it is often lifelong and compulsive,” explained Lady Scotland, a Home Office minister, in 2004. Such claims have been repeated so often that they have acquired the ring of truth. They are mostly false.

Men convicted of sex offences involving children are not, in fact, all that likely to commit further crimes. Of those released in 2002, 17% were in trouble again within two years. That may sound appalling, but compared with other ex-cons, sex offenders were paragons of virtue. The re-conviction rate for all criminals was 60% (see chart). Most incorrigible were men who stole from vehicles, 85% of whom had been re-convicted within the same period.

It is also likely that most of the child sex offenders who got into trouble after their release were collared for a different (and less appalling) crime. A study by America's Department of Justice found that, while 39% of

child molesters were arrested again within three years of release, just 3% were suspected of another sex crime against a child.



Some convicted child molesters will have returned to their old ways and not been caught, of course. Others will have lapsed later, so their crimes will not show up in the statistics. But the same is true of other criminals. And the police presumably keep closer tabs on sex offenders than on, say, burglars—otherwise, what is the point of all those lists?

Increased scrutiny may be one reason why child abusers are so much more likely than other criminals to go straight after their release. But it turns out that they often behaved themselves even before the sex offenders' register came into being in 1997. A Home Office study of men released in 1987 found that sex offenders were re-convicted at about half the average rate.

Contrary to the popular view, sex offenders can be treated. Don Grubin, a Newcastle psychiatrist, says that anti-depressant drugs and therapy seem to reduce the chance that a convict will offend again. And the mere fact of conviction may be enough to change minds. Unlike burglars and armed robbers, child abusers often suffer from the delusion that what they do is acceptable. A spell in prison, where they have to be protected from other inmates, will swiftly disabuse them of that notion.

Colin Pritchard, a psychiatrist who has studied paedophiles, says they are a diverse bunch. Most are “pathetic nuisances” who grope children but commit no other crimes. They respond well to treatment and are unlikely to re-offend. A smaller but much more dangerous group consists of men who, like Mr Huntley, are both abusive and violent. They are harder to treat, and more likely to re-offend—so much so that Mr Pritchard believes they should not necessarily be let out of prison.

Ms Kelly announced on January 19th new laws banning for life all teachers with child sex cautions as well as convictions, unless they appeal successfully. Given the low threat posed by many such people, this may be unnecessary. It would be better to focus on a small number of violent offenders. It might also be wise to worry less about teachers and more about threats closer to home. Several studies have shown that between two-thirds and three-quarters of abused children suffer at the hands of relatives or family friends.

Such a change in policy would be desirable, that is, if the intention were truly to protect children. The evidence of the past week suggests there may be more enthusiasm for heaping misery upon sex offenders and education secretaries.

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Rows in Parliament

Kelly in the lions' den

Jan 19th 2006
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The cabinet's youngest member saves her skin

PA

Fighting for her life

IT IS a bad sign when the prime minister pledges his “full support” to a cabinet colleague. If the chancellor feels moved to add his weight, the situation is dire. Ruth Kelly, the education secretary at the centre of the row over sex offenders cleared to teach, was assured of both men's backing this week as she fought to handle the explosive affair.

Hanging on her performance in the House of Commons on January 19th was not only her own immediate future but also the prospects for Tony Blair's school reforms. As *The Economist* went to press, it looked as if she had saved at least the former.

It is not clear that Ms Kelly had done anything particularly wrong on sex offenders. A cannier politician would have moved faster to fix flaws in the system that were identified before her arrival. A bolder one would have flung herself into debate on the issues, rather than running before the wind of press hysteria. But Ms Kelly is inexperienced—at 36 in 2004, she was the youngest politician by a wide margin to enter a Blair cabinet. And she has had more than her share of troubles since then.

First came the revelation that she was a member of Opus Dei, the secretive Catholic organisation that has gained notoriety from an absurd but widely-read novel, “The Da Vinci Code”. Ms Kelly rejected calls to sever her links or quit her job, saying that she was entitled to “a private spiritual life”.

Next, she antagonised the educational establishment. Sir Mike Tomlinson, a former chief inspector of schools, produced for her predecessor a plan to overhaul secondary education, boosting vocational qualifications and replacing A-level exams with a new diploma. But Mr Blair decided that he did not want to go into the elections of May 2005 with a commitment to abolish the A-level “gold standard”. Ms Kelly shelved the report, to howls of rage from many teachers.

Since then, under pressure from a prime minister hurrying to complete his reform agenda, hostile teachers and civil servants who mutter that this mother of four refuses to take work home at night, she has struggled to impose her authority. Should she survive the next few days, she faces an even greater test in February, when the government publishes its new education bill.

Mr Blair believes that schools must be set free from local authorities to innovate and compete, improve or die. Up to 90 Labour MPs threaten to vote against the bill, convinced that the reforms will benefit mainly middle-class children. Meanwhile, David Cameron, the new Tory leader, promises, embarrassingly, to rescue Mr Blair from his mutinous backbenchers and support the bill.

It is a situation that would test a seasoned heavyweight. Ms Kelly, who is neither, has sounded nervous and unconvincing in defending the proposals. Her statement on sex offenders is likely to win her some breathing space. Mr Blair might wish for a more robust spokesman for his reforms, but removing Ms Kelly now would only give encouragement to his foes.

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Productivity

Going nowhere

Jan 19th 2006
From The Economist print edition

The slide in labour efficiency is bad news for growth and the Treasury

Get article background

EVER since he became chancellor of the exchequer in 1997, Gordon Brown has made it his mission to improve Britain's productivity. He has introduced all sorts of measures to achieve this goal, ranging from tax incentives for corporate research and development to a beefed-up competition regime. Judging by the latest figures, however, he might just as well have spent the time banging his head against the wall that separates him from his neighbours in 10 Downing Street.

Output per hour worked went precisely nowhere in the year to the third quarter of 2005: the zero growth in hourly productivity was the worst performance since the series started in 1992. Output per worker rose by a mere 0.4% over the same period, the slowest rate for 15 years.

It is a far cry from the heady optimism of only a couple of years ago, when productivity accelerated sharply. Since the mid-1990s, when America improved its performance by exploiting the leap forward in information technology, the hope has been that Britain would follow suit, closing the productivity gap with many of its peers (see article). The upturn in hourly output in late 2003 and early 2004 was greeted in some quarters as the long-awaited breakthrough.

Now it appears that it was a purely cyclical phenomenon driven by economic recovery, as sceptics argued at the time. By that token, the current poor performance may also prove largely cyclical, a view backed by the Bank of England. Economic growth has slowed during 2005 to 1.6-1.7% a year, its lowest since early 1993.

But not all the productivity shortfall can be attributed to the downturn. The last time the economy was especially weak, in the second half of 2001 and the first half of 2002, GDP growth reached a low of 1.8%. Yet productivity growth then held up better than in 2005 (see chart).

"Labour hoarding" is one reason put forward to explain productivity's current poor performance. Employers are supposedly hanging on to staff during what they expect to be a short-lived stretch of economic weakness. Yet this argument is difficult to reconcile with the fact that employment rose by 1.3%, and hours worked by 1.7%, over the same period that hourly productivity failed to grow at all.

A closer look at the productivity figures reveals a structural as well as a cyclical slowdown. Hourly labour productivity grew by 2.1% a year from early 1992 to late 2005. The long-term rate of increase disguises a worrying deterioration in the past four years, however. Annual productivity growth averaged 2.3% until the third quarter of 2001, the previous low point. Since then, it has slipped back to 1.7% a year.

It is not hard to think of reasons why Britain's performance has got worse. One way to boost productivity is to equip employees with more capital. Business investment, which grew vigorously in the seven years to 2000, has been notably weak in the past five years. Labour ministers have piled regulatory burdens on firms, increasing costs and sapping entrepreneurial zest. Business is also a favourite target for Mr Brown's stealth taxes. Worst of all, firms are having to tackle big pension-fund deficits,

leaving less money available to invest in plant and equipment.

While the business sector has suffered at Labour's hands, the public sector has been showered with money. Since 1999-2000, government spending has risen by a staggering five percentage points of GDP. The public services employ only a fifth of all workers but have been responsible for nearly half the increase in the total number employed in the past five years.

The switch in resources from the private to the public sector was always likely to lower overall productivity growth since it is difficult to raise efficiency in labour-intensive services such as education. Yet the damage has been even worse than expected. In the National Health Service, for example, which has devoured so much extra cash, efficiency has been declining by about 1% a year.

The deterioration in labour efficiency overall is a particular worry for Mr Brown, for productivity growth is the mainstay of the economic expansion that in turn underpins the public finances. In its pre-budget report in December, the Treasury estimated that the trend rate of GDP growth from the end of 2006 would be 2.5% a year. Most of this was expected to come from an increase in hourly productivity of around 2.2%. That now looks too optimistic.

The productivity slowdown should also worry David Cameron, the Conservatives' new leader. One of his favourite soundbites is about sharing the proceeds of growth between the taxpayer and the public services. But if trend productivity has slowed, there will be less growth to divvy up. Only if the public services become more efficient will it be possible to avoid harsh fiscal choices.

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International comparisons

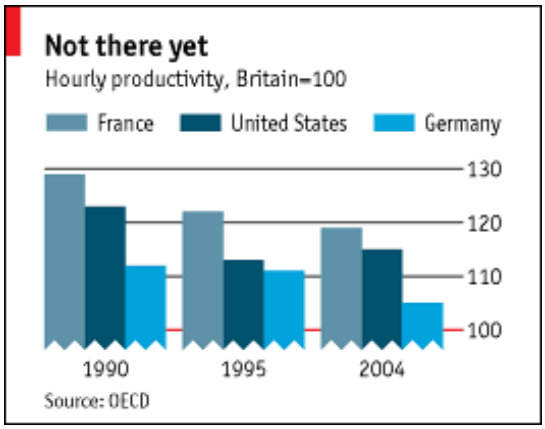
Poor show

Jan 19th 2006
From The Economist print edition

Britain has yet to catch up with its rivals on productivity

Get article background

GORDON BROWN, the chancellor, has long wished to close Britain's productivity gap with other countries. It is proving a long haul. In 2004, output per hour worked was 19% higher in France, 15% higher in America and 5% higher in Germany than it was in Britain.



It used to be worse, where Britain's big European neighbours are concerned. As the chart shows, the gap with France and Germany has been reduced since 1990. Unfortunately, this owes more to a deterioration in their performance than to an improvement in Britain's. The gap with America, by contrast, has opened up again since 1995. Firms there invested heavily in new technology and saw output per hour soar as a result, although it is slowing now.

Why is Britain finding it so hard to reach the same productivity levels as other advanced economies? A recent survey by the OECD highlighted failings in skills, innovation and transport.

Long-standing deficiencies in education mean that the British workforce has a much higher share of low-skilled people than is the case in most other developed countries. That may also explain why Britain has not wrung as much extra efficiency from its investments in technology as America.

Innovation is especially important in propelling productivity in advanced countries. But across a range of indicators —including spending on research and development, and securing new patents—Britain compares poorly with the best-performing countries.

A clogged transport system caused by years of underinvestment also seems to be harming productivity. Britain has the most congested roads in the European Union. This adds to business costs while making it difficult to reap the benefit of just-in-time production methods. Unreliable trains take their toll of commuters.

Mr Brown has plenty of ideas for tackling these and other problems. But while some of his initiatives have been helpful, the overall direction of policy has been to place new burdens on business. He rightly seeks to promote enterprise, so important in explaining America's superior productivity. But a meddling government that thinks it has the answer to everything cannot truly nurture get-up-and-go.

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Selective education

A comprehensive mess

Jan 19th 2006
From The Economist print edition

Why Northern Ireland should keep its grammar schools

EARLY rejection cuts deep. Despite his many houses, flats and Jaguars, John Prescott, the deputy prime minister, is still bitter about the bike his father would have given him in 1948 had he passed his 11-plus exam and got into grammar school. Martin McGuinness, Sinn Fein's chief negotiator, likewise failed his 11-plus and went to a secondary modern school. He remembers the exam as a "trauma".

Both men have since been able to take their revenge. Mr Prescott is one of those undermining Tony Blair's attempts to allow English schools more freedom, including in admissions. Mr McGuinness, in almost his last act as Northern Ireland's education minister before the devolved government was suspended in 2002, announced that academic selection, still used across Ulster, was to be abolished—despite the fact that more than 80% of the public want it retained in some form.

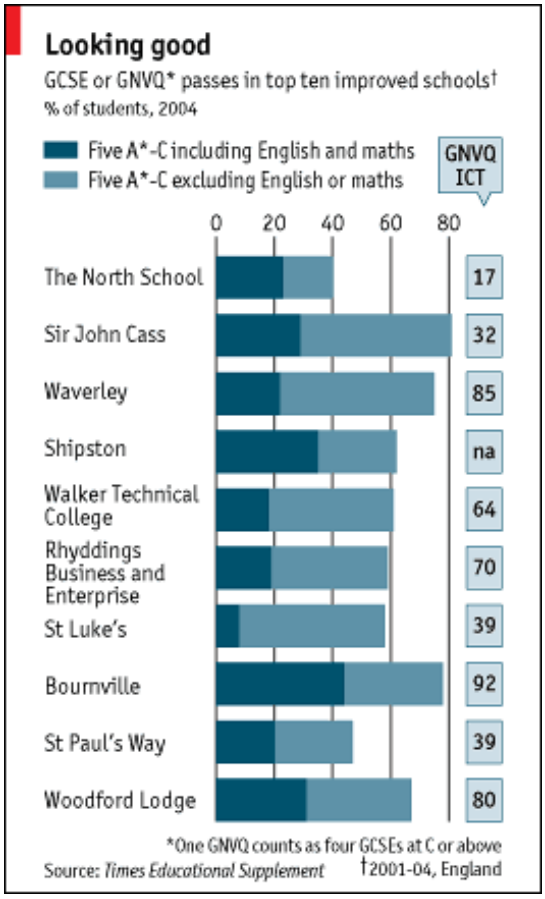
On January 16th the Association for Quality Education, a newly formed lobby group in Northern Ireland, launched a campaign to allow grammar schools to retain some sort of academic selection. "Martin McGuinness announced a policy without the approval of colleagues," says their spokesman, Sir Kenneth Bloomfield, chairman of the board of governors of a big Belfast grammar school. "But to make it effective he would have had to pass a law—and the Northern Ireland Assembly wouldn't ever have passed such a law." He rehearses the arguments wearily: private education is rare in Northern Ireland; property prices near popular schools don't soar; and the two big Belfast universities educate far more poor students than comparable universities in England.

Opponents of academic selection are unmoved—including the government, which intends to implement Mr McGuinness's decision while the province remains under direct rule. They say that poor children, disproportionately many of whom fail the 11-plus, find their chances in life damaged by the restricted syllabus on offer in secondary moderns. They see comprehensives, educating each child according to his needs, as the solution.

The 2005 GCSE-level league tables for English schools produced this week appear to show the biggest annual improvement across all schools in a decade. But an analysis of 2004 data published on January 13th provides a more sobering view of how some comprehensives are responding to the pressure for better results. Most of the 100 "most improved" comprehensives achieved their meteoric rise up the league tables by rejecting the traditional academic qualification, the GCSE, in favour of General National Vocational Qualifications (GNVQs). At many of the schools, most students did GNVQs in computing or science; very few took GCSEs in modern languages, history or science, or got good grades in English and maths (see chart). At some, GNVQ science was the only science course offered, even though it does not prepare students for A-levels in the subject.

To count in the league tables, a student must get at least five "good" GCSEs (grade C or above). A GNVQ counts as four good GCSEs, despite taking about the same classroom time as one GCSE and being far easier to pass. So the temptation, particularly for schools with less promising intakes, is silently to abandon difficult academic subjects for easier vocational ones. By 2007 the government will be piloting new "functional" skills modules in maths, English and ICT, and these may replace GCSEs as the core qualifications.

The researchers warn that the children attending these “most improved” schools—which are overwhelmingly in very poor areas—are being offered an impoverished curriculum, and will find it harder than their wealthier peers to progress to academic A-levels and traditional degree courses, regardless of their potential. So some poor English children are ending up in what are secondary moderns in all but name—and without an 11-plus to offer an escape route.



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Prostitution

Lights out

Jan 19th 2006
From The Economist print edition

New laws for an old profession

LIKE a Victorian evangelist, the British government wants to rescue women from sexual bondage. According to a new plan, unveiled on January 17th, streetwalkers will be pushed into treatment for the drug addictions most of them are thought to have. Trafficked and pimped women will be rescued. Punters who cruise red-light districts will be vigorously prosecuted and publicly shamed. Although, as a Home Office minister admitted, “we are not going to eradicate prostitution overnight,” the hope is that it will disappear eventually.

To those who work in the vice trade, such schemes are no more likely to succeed than those of the 19th-century moralists, and are about as removed from the reality of the modern sex business. Marie, who runs a massage parlour in the Midlands, is indignant at the latest calumny on her profession. Women who work the streets may well be drug-addled, she says. But her staff consists entirely of “average, everyday ladies earning a wage”.

In the past decade, two forces have transformed the business of prostitution. The first is technology. Mobile phones and the internet have made it easier for supply and demand to get in touch, so prostitutes no longer have to stand on street corners, touting for custom and annoying the neighbours.

The second force is immigration. Eastern Europeans (few of them trafficked, despite the horror stories) have flooded into the sex trade. The increase in supply has had the expected effect on prices. George McCoy, the author of a guide to massage parlours, says that prices have held steady or fallen for several years. In Marie's city, a half-hour “full service” costs just £40.

Massage parlours are much safer than the streets, as even the government admitted this week. (Along with the tough stuff, it proposed to loosen a law that, at present, makes it illegal for several women to ply their trade from the same address.) But these dens of vice are not just good for those who work in them. Competition from massage parlours is a big reason why prostitutes have virtually disappeared from the streets of many cities, including London. So far, the invisible hand of the market has done more to push women out of the most dangerous kinds of sex work than has the heavy hand of authority.

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Britishness

Gordon's history lesson

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From The Economist print edition

The chancellor defines Britishness, the British National party shouts back

FLAG-WAVING has long been distasteful to left-wingers in Britain. That is partly because the internationalism that runs through the history of the Labour Party sits awkwardly with the Union Jack, symbol of empire. But it is also because the right just seems to do patriotism better.

New Labour is trying to change this, and the chancellor of the exchequer is trying harder than most. In a speech on January 14th—his latest of several on the subject—Gordon Brown mused on the beauty of fluttering flags in Britain's back gardens. He talked about the danger of letting "the old left's embarrassed avoidance of an explicit patriotism" grant white supremacists a monopoly on the Union Jack.

As if to prove his point, Nick Griffin, the leader of the British National Party (BNP), went on trial two days later for his own kind of flag-waving. Mr Griffin thinks that immigration and crimes against whites have turned Britain into "a multiracial hell-hole", and that the only remedy is to kick out all the "ethnics". He is in court charged with stirring up racial hatred.

Up against that sort of rhetoric, Mr Brown's version looks rather grey. Britishness, he thinks, is not about common blood and culture, about dreaming spires and the changing of the guard, but is based on a sober set of shared values. Where the French have *liberté*, *égalité* and *fraternité*, and Americans the right to life, liberty and the pursuit of happiness, Mr Brown's Britain thrills to "liberty for all, responsibility by all and fairness to all".

This may not be the stirring stuff of barricades. It also takes a deft reading of history to show that the sweep of the past 2,000 years has led precisely to the values of New Labour's third term. And any Scot who wants to be prime minister of Britain is certainly well advised to talk up the wonders of the union.

But plenty of Britons agree with Mr Brown that Britishness stands for shared values rather than a shared heritage. The strength of this feeling, though, is divided along racial lines: 61% of non-whites told a poll by YouGov for the Commission for Racial Equality that Britishness is about values such as the rule of law and fair play rather than about heritage, while only 27% of whites felt the same way.

Can the government foster a feeling of Britishness? Though half of those surveyed in a separate YouGov poll agreed that "it's not the role of politicians to come up with what being British means," history suggests that it can. It was, after all, a (Roman) government that gave the name Britannia to a rather nondescript province on the northern edge of its empire. Another government innovation, the Act of Union in 1707, gave a big boost to "Britain" (as opposed to England, Scotland, Wales or Ireland). The creation and expansion of a British empire (which Mr Brown downplayed) helped too.

Three of the chancellor's many suggestions for increasing a shared and patriotic national awareness stand out. Language—so obvious, perhaps, that hardly anyone mentions it—is a unifying force. Increasing efforts to make all Britons fluent in English is surely a good idea. So is teaching British history (including the awkward imperial bits) in a way that explains how so many different tribes wound up living together on a smallish island—rather than jumping from stray bits on the Tudors to the 20th century's world wars.

Less compelling is his hint that a day could be set aside for flag-waving. One abiding feature of Britishness is a reticence about overt demonstrations of patriotism: flags are seen on Remembrance Sunday, at sporting events and occasionally as bedspreads. And there is a technical problem too. "A proper Union Jack," says Charles Ashburner, who runs Mr Flag, a flag-maker and supplier, "is made up of 32 pieces of material sewn together by hand. It's a dying art." Both Mr Brown and Mr Griffin will soon have to make do with cheaper versions printed in

China.

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Bagehot

Cameron's way

Jan 19th 2006
From The Economist print edition

The Conservative leader has set a new direction for his party. Will it follow him?

Get article background

A COUPLE of weeks ago, David Cameron and his wife, Samantha, were conveniently spotted going into a cinema showing “Brokeback Mountain” on the first day of its release.

The new Tory leader's choice of film, a Western that depicts a homosexual relationship both graphically and sympathetically, gave useful reinforcement to everything he is trying to do with his party. Gay-rights campaigners, who until recently would have shunned the Conservatives, have been quick to salute Mr Cameron. A website called pinknews.co.uk gushed: “David Cameron is the leader of the future. Young gay professionals are the perfect group of people to support the Conservatives.”

It is now just over six weeks since Mr Cameron was elected leader by a two-to-one majority and his initial strategy has become clear. He has three interlocking aims. The first is to deal quickly and decisively with what the party chairman, Francis Maude, calls the Tories' brand problem. During the last election, the party discovered that once a policy was identified with the Conservatives, it automatically became unpopular with voters even if they had approved of it before its attribution.

The second is to establish a clear sense of direction that will inform detailed work on policy. The third, according to Oliver Letwin, who is in charge of the policy review, is to “buy the right” later on to have radical ideas taken seriously. That can only be done by changing perceptions of the party's motives—above all, the belief that Tories are mean-spirited and selfish.

Without anything as significant symbolically as Labour's pro-nationalisation Clause Four to scrap, Mr Cameron has chosen to move on multiple fronts. Some of the things he has done smack of gimmickry, such as recruiting the poverty campaigner Bob Geldof and the green activist Zac Goldsmith as policy advisers (he even tried to enlist one prominent Labour backbencher). But the series of speeches he has made since becoming leader have been deadly

serious in their intent.

Portrayed in much of the press as a rejection of long-held Tory principles and policies, the speeches have earned Mr Cameron glowing praise from liberal newspapers and ill-tempered suspicion from their right-wing counterparts—exactly what he had hoped for. But what makes them so clever is the impact they have had without Mr Cameron saying anything extraordinary.

It is true that the Tory leader has explicitly ruled out any return to the 11-plus selection exam or the creation of new grammar schools. It is also true that he has committed himself to maintaining the existing tax-funded financing for the health service. But in 18 years of Tory government before 1997 not a single new grammar school was opened, nor did even Margaret Thatcher challenge the funding principles of the NHS.

Yet some Tory commentators and think-tank intellectuals have condemned Mr Cameron for abandoning sacred Conservative values, which is some indication of how far the party had drifted from mainstream political opinion. There are arguments both for academic selection and insurance-based health systems, but there is little evidence that British voters are interested in hearing them—least of all from the Tories.

The break that Mr Cameron's speeches mark is with the years of Tory failure rather than the years of Tory success. They do not rule out, as some critics have claimed, applying a market-based approach to the provision of public services or reinvigorating the supply-side of the economy. What they do demonstrate is that in politics how you say things is as important as what you say.

Already, Mr Cameron's attempt to find a different language is yielding results. The most recent opinion poll (conducted by ICM) gives the Tories a 39% share of the vote and a four-point lead over Labour—according to ICM's data, the best position the Tories have held since sterling fell out of Europe's currency systemin 1992. A Populus poll last week found that Mr Cameron had already gone a long way towards neutralising the Tories' negative brand image. In some instances, knowing that a statement came from him actually increased people's support for it.

The shock of the new

It was against that promising background that Mr Cameron held on January 17th the first private meeting of Tory MPs since the beginning of his campaign to re-position the party. Anyone hoping for rebellious rumblings will have been disappointed. Apart from one slightly barbed question about the extent to which the supposedly consultative policy commission had been pre-empted by the leader's speeches, there was near-euphoria. Even those on the hard right who are uncomfortable with the direction Mr Cameron has plotted for the party are reluctant to challenge the mood of optimism he has generated.

Whether that will survive the outcome of Mr Letwin's policy review in 18 months' time is another matter. Tony Blair, for one, thinks that Mr Cameron will either be dragged further to the right than he intends or face real difficulties with his party. Unlike Labour's left wing, the Tory right, Mr Blair argues, does not in its heart of hearts know that its ideas are vote-losers. He promises that Labour's attack, when it comes, will be based on Mr Cameron's actions rather than on his soothing words.

But that will come later. For now, the danger for Mr Cameron is that people expect too much of him. So far, the Tory advance has come at the expense of the self-destructing Liberal Democrats. Soon, he must show he can inflict lasting damage on the government. If he maintains his momentum, his party will allow him to take it wherever he wants. If he does not, the doubts could grow quite quickly.

Mr Cameron's strategy of popping up all over the place sounding terribly decent and looking as if he belongs in the 21st century is working a treat and he is carrying it off with elan. But when the shock wears off, will he know what to do next?

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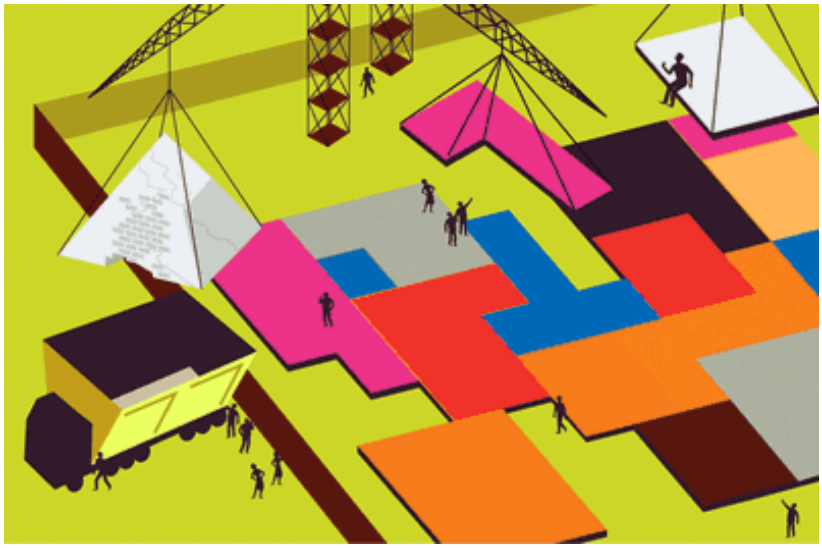
BARCLAYS See how we can help plan for your future

The new organisation

Jan 19th 2006
From The Economist print edition

The way people work has changed dramatically, but the way their companies are organised lags far behind, says Tim Hindle (interviewed here)



FIFTY years ago William Whyte, an editor at *Fortune* magazine, wrote a book called “The Organisation Man” that defined the nature of corporate life for a generation. The book described how America (whose people, he said, had “led in the public worship of individualism”) had recently turned into a nation of employees who “take the vows of organisation life” and who had become “the dominant members of our society”.

Foremost among the organisations that Whyte had in mind was the corporation, which he thought rewarded long service, obedience and loyalty quite as faithfully as did any monastery or battalion. “Blood brother to the business trainee off to join DuPont is the seminary student who will end up in the church hierarchy,” he wrote. The *New York Times* praised Whyte for recognising that “the entrepreneurial scramble to success has been largely replaced by the organisational crawl.”

Half a century on, organisation man seems almost extinct, though occasionally he can still be spotted in Hollywood. In “The Hours”, a 2002 Oscar-winning film, the actor John Reilly plays a character who lives in a 1950s Los Angeles suburban bungalow, just as Whyte's organisation man lived in “the new suburbia, the packaged villages that have become the dormitory of the new generation of organisation men”. Mr Reilly is waved off to work every morning by his young son and his faithful wife, played by Julianne Moore. His shirt is white and his suit and tie are dark, broken only by the line of a white handkerchief in his breast pocket. He spends all day in an office with the same small group of people and returns home each evening at the same time. “This is perfect,” he says of his life over dinner one evening.

The company that used to be most closely identified with this way of life was IBM. For many years its managers wore only dark blue suits, white shirts and dark ties, symbols of their lifetime allegiance to Big Blue. It is some measure of the change that has taken place since Whyte's day that today 50% of IBM's employees have worked for the company for under five years; 40% of its 320,000 employees are “mobile”, meaning that they do not report daily to an IBM site; and about 30% are women. An organisation that was once dominated by lifetime employees selling computer products has been transformed into a conglomeration of transient suppliers of services. Organisation man has been replaced by a set of managers much more given to entrepreneurial scramble than to organisational crawl.

This transformation has been brought about by a variety of changes in the environment in which businesses

operate, particularly in communications technology, in the globalisation of production and sales, and in the large-scale shift of responsibility to outsiders for what were once considered a company's core functions—via outsourcing, joint-ventures and other sorts of alliances that involve a loosening of control over vital inputs.

Whyte, who died in 1999, would have enjoyed witnessing organisation man's metamorphosis into “networked person”, a species that can now be observed in airport lounges, on fast inter-city trains and at motorway service stations. Networked person is always on the move, juggling with a laptop computer, a mobile phone and a BlackBerry for e-mails, keeping in electronic touch with people he (and increasingly she) no longer regularly bumps into in a corridor. Indeed, there may be no corridor. These days, many employees besides IBMers no longer have a physical home base in a building provided by their employer.

Organisation man did bump into people in corridors, but he was cautious about networking. In his world, knowledge was power, and he needed to be careful about sharing out his particular store of it. He found comfort in hierarchy, which obviated the need to be self-motivating and take risks. He lived in a highly structured world where lines of authority were clearly drawn on charts, decisions were made on high, and knowledge resided in manuals.

Networked person, by contrast, takes decisions all the time, guided by the knowledge base she has access to, the corporate culture she has embraced, and the colleagues with whom she is constantly communicating. She interacts with a far greater number of people than her father did. A famous 1967 study by Stanley Milgram (which later became the basis for a film) suggested that there were at most “six degrees of separation” between any two people in America, meaning that the chain of acquaintances between them never had more than six links. According to more recent work along similar lines, that number has now fallen to 4.6, despite the growth in America's population since Milgram's study. Being able to keep in touch with a much wider range of people through technologies such as e-mail has brought everyone closer.

And yet despite the dramatic changes in the way people work, the organisations in which they carry out that work have changed much less than might be expected. In an article in the *McKinsey Quarterly* last year, Lowell Bryan and Claudia Joyce, two of the firm's consultants, argued that “today's big companies do very little to enhance the productivity of their professionals. In fact, their vertically oriented organisational structures, retrofitted with ad hoc and matrix overlays, nearly always make professional work more complex and inefficient.” In other words, 21st-century organisations are not fit for 21st-century workers.

Mercer Delta, a consulting firm that specialises in “organisational architecture”, recently observed that “the models and frameworks that shaped our leading organisations from the end of the second world war through the conclusion of the cold war are clearly obsolete in this new era of e-business, perpetual innovation and global competition.” The design of today's complex enterprises, says Mercer Delta, requires an entirely new way of thinking about organisations.

The classic structure in which organisation man felt comfortable consisted of a number of business units that operated similarly but separately. They were controlled by a head office that determined strategy and watched over its implementation. It was a system of command and control in which everybody knew his place, made visible in the organisation charts that laid down the corporate hierarchy.

A surprising number of companies today still have much the same command-and-control structure that they had 50 years ago. According to the Boston Consulting Group, what it calls “the imperialist corporate centre” is still the most common type of headquarters. And companies that do decentralise decision-making and accountability often recentralise it again when they run into trouble.

Twenty years ago, Motorola, a co-inventor of the mobile phone, was a tightly centralised business. Three men in its headquarters at Schaumburg, Illinois (including Bob Galvin, the founder's son), were in control of almost everything that went on. As the company grew, they decided to decentralise. But by the mid-1990s the company's mobile-phone business was growing so fast that decentralisation made it impossible to control. “While the numbers are getting better, an organisation can be falling apart,” says Pat Canavan, Motorola's chief governance officer. In 1998 the company laid off 25,000 people and repatriated control to the Schaumburg headquarters.

The trouble with silos

The main failing of the classic structure was that it impeded the spread of knowledge and limited the economies of scale that could be reaped. Ideas and commands moved up and down from headquarters to the units, leading to the creation of vertical “silos” with very little communication between them. Financial-service institutions were notorious for not knowing whether customers who signed up for one service were already customers for other services being provided by the same institution.

As firms became more global, they added what McKinsey called a “matrix overlay” to this structure. Most famously associated with Philips, a Dutch electrical and electronics giant (see article), this attempted to take more account of the different national markets in which a company was operating by superimposing geographical silos that cut across the traditional business units.

Such organisations have not commanded universal admiration. In 1990, in a paper published by the *Harvard Business Review*, Sumantra Ghoshal and Christopher Bartlett, two academics, reported that matrix structures “led to conflict and confusion; the proliferation of channels created informational logjams as a proliferation of committees and reports bogged down the organisation; and overlapping responsibilities produced turf battles and a loss of accountability.” Nigel Nicholson, a professor of organisational behaviour at the London Business School, called the matrix structure “one of the most difficult and least successful organisational forms.”

Messrs Ghoshal and Bartlett wrote in the past tense, suggesting that companies had escaped from the matrix corset. But 15 years after the article was published, many are still trying to struggle free.

Gerard Fairtlough, a former CEO of Shell Chemicals and the founder of Celltech, a British biotechnology company, also suggests that companies are still being held back by their addiction to hierarchy. In a recent book, “The Three Ways of Getting Things Done”, he points to alternatives to the hierarchical structure that many companies see as their only option.

“You can't have a bunch of hippies running a plant full of explosive hydrocarbons,” he says. “But would you rather have the plant operated by trained professionals, for whom pride in safe working is part of their personal identity, or by people who only work safely because they are afraid of the boss? The identification of discipline with hierarchy is a dangerous mistake.” Mr Fairtlough's preferred alternative is something he calls “responsible autonomy”, a form of organisation in which groups of workers decide for themselves what to do, but are accountable for the outcome.

Clearly there is a need for new kinds of organisation that are more appropriate to modern working methods. But there are many reasons why companies are not in a hurry to adopt them.

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The matrix master

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From The Economist print edition

Philips redraws the lines

PHILIPS, a Dutch electrical giant, was one of the earliest champions of the matrix structure. After the second world war it set up both national organisations and product divisions. The boss of the washing-machine division in Italy, say, would report to the head of Philips in Italy as well as to the washing-machine supremo in the Netherlands. This network was loosely held together by a number of co-ordinating committees designed to resolve conflicts between the two lines of command.

By the 1990s Philips had decided that this structure was no longer working well. There had been more or less continual problems over accountability. Who was to be held responsible for the profit-and-loss account—the country boss or the product head? For a while, the country heads had had the upper hand, but the product bosses had fought back. A reorganisation in the early 1990s created a number of units with worldwide responsibility for groups of the company's businesses—consumer electronics, medical products and so on. The national offices became subservient to these new units, built around products and based at the firm's headquarters.

Gently does it

In the past three years the company has been gently drawing back from this structure without attempting a radical reorganisation. For instance, it has appointed a chief marketing officer to help counter the criticism that it has been paying too much attention to technology and new products and not enough to its customers.

Gerard Ruizendaal, head of corporate strategy at Philips, says the company has learnt that whenever it creates a new organisation, it creates a new problem. So, under the slogan “One Philips”, it has introduced a number of low-key changes, such as encouraging employees to work across different business units. In November, it handed out awards for three business initiatives in which people had created value for the company by collaborating with others outside their immediate units.

Philips is also making it clear that employees are expected to move around in their careers rather than stick with a single geographical region or product area. Mr Ruizendaal says that 70-80% of the changes required will come about by shifting managers' attitudes; the rest from putting in place incentives, not all of them monetary. To help change minds, Philips last year brought together its top 1,000 managers for a series of workshops expressly designed to talk about issues that cut across organisational boundaries.

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Take a deep breath

Jan 19th 2006
From The Economist print edition

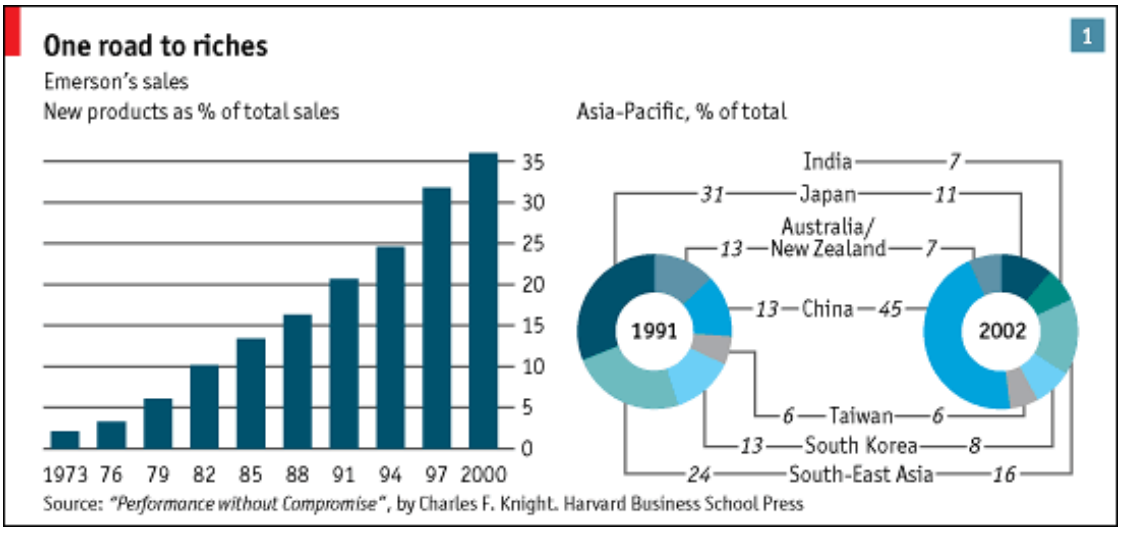
The best time to embrace radical change is when you are down

ONE reason why so many companies stuck to their old organisational structures for so long is that they still seemed to be working. General Electric under Jack Welch was one example. Emerson, an electric and electronics business based in St Louis, was another.

Emerson's story was recounted last year in “Performance without Compromise”, a book written by Charles “Chuck” Knight, the man who led the company through most of an unbroken run of continually rising earnings per share between 1957 and 2000. At first sight, Emerson looks like a company in which organisation man would feel at home. “Planning and control are central to the way Emerson works,” according to Mr Knight. More than half his time was taken up with planning, much of it spent in long, confrontational meetings with the company's division heads, where budgets and projections were torn apart and redrawn. This compelled the company to maintain a relatively large number of staff at its headquarters in St Louis.

Emerson's employees are loyal. The average length of service of its top 15 managers is a hefty 26 years, and promotion tends to be from within. Communication, says Mr Knight, is kept to a minimum: “Our planning and control cycle provides ample opportunity to communicate the most important business issues...we don't burden our system with non-essential communications and information.”

The company's success was, on Mr Knight's own admission, the fruit of a long, hard slog. A little light relief was provided by an annual golf tournament for top executives and important customers—“a great way for our people to bond with each other,” according to Mr Knight. Not surprisingly, the Emerson story features very few women. All in all, the company sounds like the sort of command-and-control organisation that has outlived its effectiveness.



Yet Emerson continues to be successful. Its secret seems to be that, notwithstanding the title of Mr Knight's book, it has in fact been prepared to compromise. In the 1990s, for example, the company set up account teams to deal with big customers who bought from several of its divisions. The teams cut across the company's long-standing organisational boundaries. The purpose, says Mr Knight, “was to allow the customer to see Emerson as a single integrated supplier rather than a collection of independent divisions.”

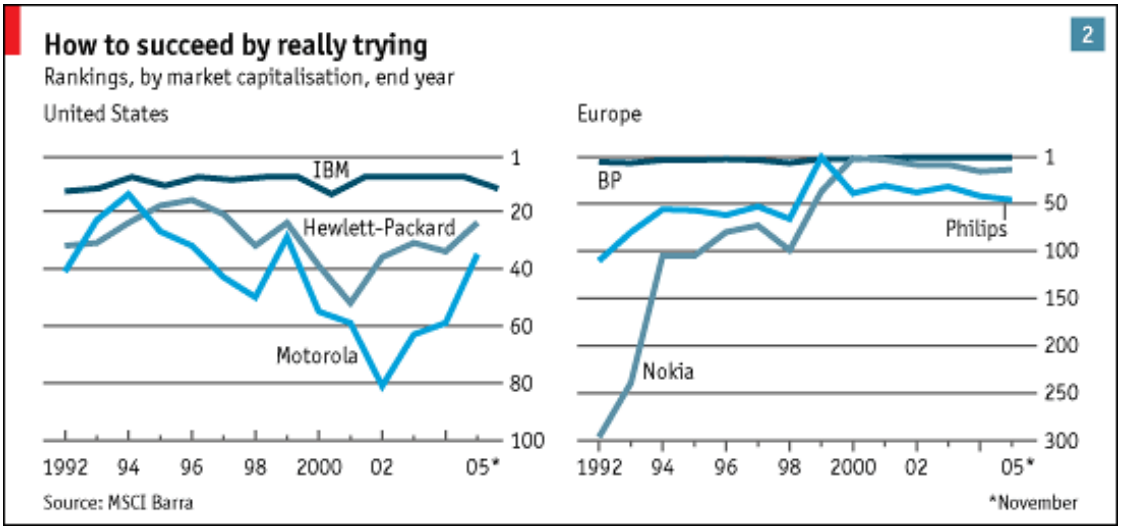
The company has also set up a design-engineering centre in India, invested heavily in China and hired some of the most progressive advisers on strategy and leadership development. Its current CEO, David Farr, spends more time with customers than did his predecessor. In short, Emerson, despite first impressions to the contrary, has changed

quite a lot over the years. As Mr Knight puts it: “We succeeded in combining impressive consistency *and* fundamental change” (his emphasis).

The uses of adversity

By and large, though, successful companies find it a lot harder to restructure than those that have less to lose. Organisations are strongly inclined to carry on with “the way things are done around here” unless they have compelling reasons to stop. It is little wonder, therefore, that many of the recent pioneers of new organisational structures were in deep distress when they introduced them.

One example is BP, an international oil giant that was close to bankruptcy in 1992 when Lord (John) Browne, then head of the company's oil-exploration division (known as BPX), set out to restructure his fief. The choice was stark: radical change or extermination. In the best recent book on new corporate architecture, “The Modern Firm”, John Roberts, an economist at Stanford, describes the reorganisation at BPX as “disaggregation”.



Its key elements, he says, “involve redrawing the horizontal and vertical boundaries of the firm to increase strategic focus; creating relatively small sub-units within the organisation in which significant decision-rights are lodged; and decreasing the number of layers of management and the extent of central staff.”

Accountability and responsibility for performance at BPX were pushed down to the level of the company's individual oil fields. Previously performance measures had been aggregated by geographic region, leaving managers further down the line with little idea of how well they were doing, and little incentive to do better. When early experiments with disaggregation showed that it increased output and brought down costs, it was introduced across BPX, and then across the whole of BP after Lord Browne became CEO of the whole company in 1995.

The oil giant had traditionally had a highly centralised hierarchical structure, but Lord Browne cut its head-office staff by some 80% and pushed decision-making down to 90 newly established separate business units. The hierarchy was flattened so much that the head of each of the 90 units reported directly to the company's nine-man executive committee—though as BP subsequently grew through takeover, some intermediate layers were introduced again. Individual managers also had much of their head-office support removed. The top of their silo had suddenly been lopped off.

To discourage the silo mentality further, horizontal links were set up between the units. BPX's assets were split into four groups, roughly reflecting the stage they had reached in their economic life. Members of each group thus faced similar commercial and technical issues, and were encouraged to support others in their group and help solve each other's problems.

Mr Roberts says that these changes in “the architecture and routines eventually led to fundamental cultural changes. BP's people developed a deep, intrinsic dedication to delivering ever-improving performance. Strong norms emerged of mutual trust, of admitting early when one faced difficulties and seeking assistance when needed, of responding positively to requests for help, of keeping promises about performance.”

As part of the reorganisation, some assets were sold off and BP's total staff was cut from 97,000 in 1992 to just over 50,000 three years later. Over the past decade the company's stock has performed exceptionally well.

Like BP, Philips was in deep financial trouble when at last it began to take down its long-standing matrix structure in 1991 (see article). And IBM in 1992 recorded the biggest loss to date in corporate history, which prepared the ground for Lou Gerstner to give Big Blue a new strategy—to concentrate on services—and a new structure to go with it. Likewise, Nokia in 1992 was a hotch-potch conglomerate, with products ranging from rubber boots to television sets, and going nowhere. It switched its strategy to specialise in telecommunications and built a new structure to go with it. Today Nokia and BP are two of Europe's most valuable companies, and IBM is once again one of the world's most admired companies.

“Organisational innovations, when properly applied, do lead to better economic performance, affecting the material well-being of the people of the world,” says Mr Roberts. “Moreover, they alter the ways work is done, changing people's lives.” Structure matters. Much of the large increase in the ratio of firms' stockmarket value to their book value since the early 1990s is due to the market's growing awareness of the role of human and organisational capital in the creation of value. For companies such as Wal-Mart and Dell, their structure is their main source of competitive advantage. For companies currently in difficulty, such as General Motors and the big American airlines, structural reorganisation will be a necessary part of any recovery.

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The tortoise and the hare

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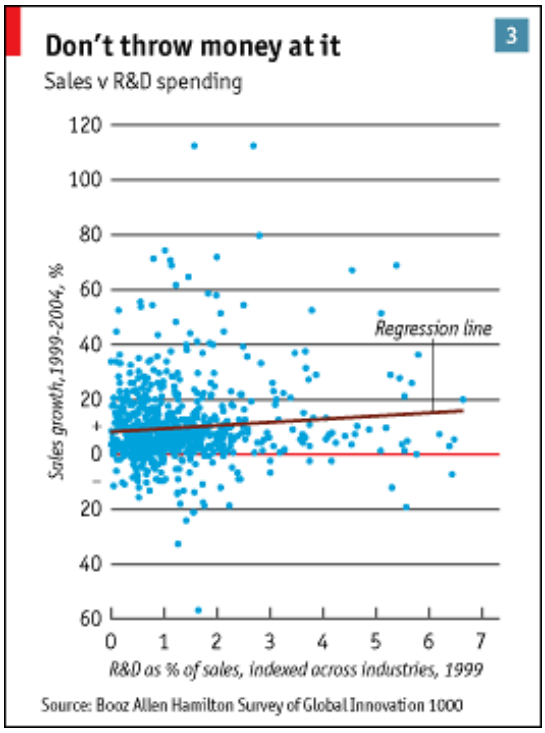
The search for innovation

WHY would a healthy and successful company want to subject itself to a long and painful process of restructuring? In telling Emerson's story, Mr Knight hints at an answer. In the early 1990s, the company decided to separate its “planning for profit” from its “planning for growth”. Previously its management's efforts had been concentrated mainly on paring costs and improving margins. But Emerson realised that it was time to “emphasise new products, new markets and new customers”.

Many companies today are in the same position. They are emerging from a long period when their main concern was to cut costs and improve their balance sheets after the dotcom bust. Squeezing costs has dramatically improved profits: in each of the last three quarters of 2005, earnings per share of companies in the S&P 500 index were around 20% up on the same period in the previous year.

Now firms are trying to expand and find new customers. They are beginning to pay less attention to their bottom-line profits and more to their top-line revenues. A recent survey by the Conference Board, an association of American businesspeople, puts “sustained and steady top-line growth” at the top of the list of American CEOs' concerns.



The fun of the new

Pushing up revenues is more fun than cutting costs. It involves doing or buying new things, and the temptation is always to do this too soon and too enthusiastically. A.T. Kearney, a consulting firm, argues that growth of revenue and of profits are interrelated. In studying the performance of a group of big global banks between 1996 and 2003, it found that very few of them were able to increase shareholder value by more than 15% per annum without increasing their top-line revenues to match. A recent study by McKinsey came up with a similar finding: that a company “whose revenue increased more slowly than GDP did was five times more likely to succumb, usually through acquisition, than a company that expanded more rapidly.” The choice for corporate bosses seems to be: grow or be gobbled.

In essence, there are two ways of achieving top-line growth: companies can buy it through mergers or acquisitions, or they can generate it internally. To do the second, they need to innovate.

In an American magazine-editors' poll last year to find the 40 best covers of the past 40 years, the single example from *The Economist*, dating from 1994, was headed “The trouble with mergers” and featured two camels coupling awkwardly. The article that went with it explained why most mergers go wrong. But mergers have become no more extinct than camels. Last year was a bumper one for cross-border acquisitions in Europe, and in America the value of telecoms deals alone was over $100 billion. Nevertheless, it remains extremely difficult to make mergers work.

There is some evidence to suggest that companies are becoming better at it. Some of them have set up special mergers-and-acquisitions units, manned by experts in the skill of post-merger integration. Motorola has introduced a systematic review of every acquisition three years after the event to see what lessons can be learnt.

What may also have helped is that with money relatively cheap, more deals today are being financed with cash than with the buyer's stocks and shares (the method favoured during the stockmarket bubble at the beginning of

this decade). This tends to concentrate buyers' minds more sharply on the value of their acquisition.

Go organic

Yet there is a limit to the amount of top-line growth that can be bought. A recent report from A.T. Kearney says that “in some industries, significant growth is still possible through acquisitions. But the unavoidable reality is that long-term advantage also requires skills at creating organic growth.” This need to create internal growth is driving companies to search for ways of making their people more creative and more productive.

The problem is particularly pressing for the big oil companies. Unless they merge with one of their own number, which may well be ruled out by antitrust considerations, no acquisition can make more than a marginal difference to their top line. Some other industries, such as food retailing in Britain, face the same dilemma. For Tesco, as for BP, the only real option for growth is organic.

At the heart of organic growth lies innovation: new ideas to develop new products and new markets. In the past, innovation took place mostly in the R&D department. In a paper written in 2001, Baruch Lev, a professor of accounting and finance at New York University, wrote: “Much of the research in the field of intangibles deals with R&D, which is just one—albeit important—form of intangibles. The reason for the R&D focus of researchers is simple: R&D is the only intangible asset that is reported separately in corporate financial statements.”

In fact, the men in white coats have not been doing very well with their new pills and gadgets in recent years. A study in 2005 by consultants at Booz Allen Hamilton, the most comprehensive effort to date to assess the influence of R&D on corporate performance, concluded that “there is no relationship between R&D spending and the primary measures of economic or corporate success.” What matters is not how many R&D dollars you spend, say the authors, but how you spend them.

Most of the innovation in pharmaceuticals these days is coming from small new firms. Big Pharma's R&D activity is now concentrated as much on identifying and doing deals with small, innovative firms as it is on trying to discover its own blockbuster drugs.

Traditionally, innovation has taken place either in the laboratory or in the marketing department. The laboratory may have proved sterile in recent years, but the marketing department has been a hive of creative activity, with endless new products and product extensions pouring out. The iPod digital music player, for instance, was quickly followed by the even smaller iPod nano; the Kit Kat chunky chocolate bar by the caramel Kit Kat chunky bar.

Yet there is a limit to this process too. In an article last year in the *Journal of Economics and Management Strategy*, Dipak Jain, dean of the Kellogg business school, and Michaela Draganska, an academic at Stanford, claimed that too many product extensions can have an adverse effect on overall market share and push up costs. Producers as well as consumers, it seems, can have too much of a good thing.

Look high and low

Where else, then, can companies turn for innovation? Many of them are now formally looking outside their own organisations. Joint-ventures and in-house venture-capital funds enable them to take a stake in potentially interesting ideas without the full risk of developing them. Motorola has four main outside sources from which it hopes to draw new ideas: universities, where it funds research in areas of interest to it; government bodies, to which it applies for research grants; small and medium-sized enterprises, from which it licenses or buys new ideas; and its own in-house venture-capital fund, some of whose investments may come up trumps.

Sometimes innovation can take unusual forms. Adrian Slywotzky, a consultant at Mercer and author of a book entitled “How to Grow When Markets Don't”, tells the story of Air Liquide, a French manufacturer of industrial gases that has been innovative in an unconventional way and has grown dramatically as a consequence. The company found itself in a mature business where it had little hope of coming up with new products. So it turned itself from a simple maker of gas into a provider of energy services to its customers (mainly large corporations), and managed to persuade many of them to outsource all their energy needs to it. For several years thereafter, Air Liquide managed to chalk up double-digit growth in both revenues and profits.

The story is reminiscent of that of IBM, which switched from being a provider of hardware to being a supplier of services to users of similar hardware. It built a new business by supplying its existing customers with something different in which it could reasonably claim expertise. Between 1994 and 2003, IBM notched up mainly organic annual growth of 15-20% in revenue from services. Over the same period, the proportion of the company's total

revenues that came from services rose from 25% to almost 50%.

All this goes to show that innovation can be a quite a simple thing. It does not reside only in the minds of brilliant but nutty scientists, or of creative luvvies in marketing departments and advertising agencies. It can blossom almost anywhere in an organisation that is properly structured to encourage it.

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Thinking for a living

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Knowledge workers need a new kind of organisation

CENTRAL to much thinking about how organisations should be restructured for the 21st century is the idea that innovation and growth will depend more and more on so-called knowledge workers, the sort of people who, to quote the title of a recent book by Thomas Davenport of Babson College, Massachusetts, find themselves “Thinking for a Living”.

Lowell Bryan and Claudia Joyce at McKinsey reckon that knowledge workers (whom they prefer to call “professionals”) “represent a large and growing percentage of the employees of the world's biggest corporations”. In some industries, such as financial services, media and pharmaceuticals, they think the share may already be as high as 25%.

Others would put it much higher. One of the secrets of Toyota's success, says Takis Athanasopoulos, the chief executive of the Japanese carmaker's European operations, is that the company encourages every worker, no matter how far down the production line, to consider himself a knowledge worker and to think creatively about improving his particular corner of the organisation (of which more later).

In one sense, the organisation in which every member is a knowledge worker already exists: it is the professional-service firm, the organisational structure favoured by lawyers, accountants and consultants. Most such firms are organised as partnerships or quasi-partnerships, where strategic decisions are made democratically at regular get-togethers of the partners.

That is not a practical way to run a multinational company with hundreds of thousands of employees in dozens of countries. But in small ways, technology is already helping big firms to treat their employees more like partners. IBM recently held a 72-hour online chat session (which it called a “jam”) among employees from 75 different countries to discuss the company's values, and plans to hold more. “Jams enable a kind of mass collaboration and problem-solving that has simply never before been possible on a global scale,” says Irving Wladawsky-Berger, the company's vice-president of technical strategy and innovation.

McKinsey's Mr Bryan soberly points out that we are not all knowledge workers yet. “Fifty per cent of workers are still modern versions of old-style factory workers,” he says. They still live off their brawn rather than their brain, and they may be able to live happily with organisational structures that are, as Mr Bryan puts it, “retrofitted with ad hoc and matrix overlays”, and that are ill-suited for knowledge workers. Today's complex firm may need a new matrix, with one structure for its knowledge workers and another for its more traditional workforce.

However defined, the knowledge worker is not exactly a new invention. In one of his more prescient moments, Peter Drucker, the great management thinker who died last November, wrote: “To make knowledge-work

productive will be the great management task of this century, just as to make manual work productive was the great management task of the last century." The date was 1969, and by "this century" he meant the 20th.

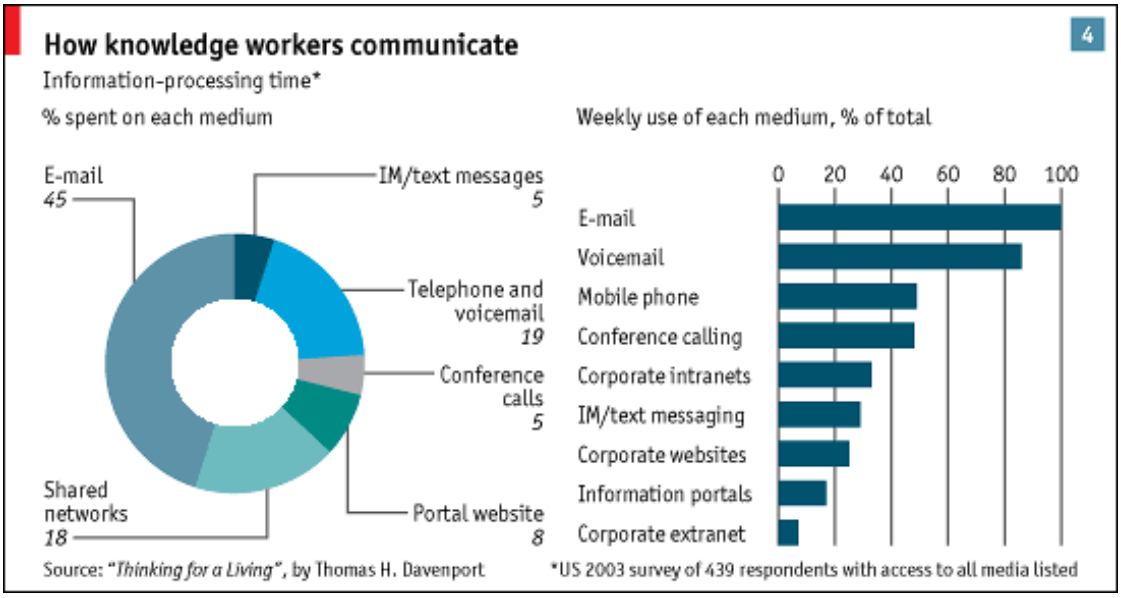
Taylor-made

The task he referred to had been begun by Frederick Winslow Taylor, an American Quaker who had devised what he called "a piece-rate system" while working for the Bethlehem Iron Company in the late 19th century. Drucker said that Taylor was the first man who "did not take work for granted, but looked at it and studied it." Through his study, he "sparked the revolution that allowed industrial workers to earn middle-class wages and achieve middle-class status despite their lack of skill and education".

Drucker was calling for another revolution, one that would make knowledge workers more productive, but he was still waiting for it when he died. Mr Davenport puts his finger on one of the key problems: measuring the output of knowledge workers. How, for instance, do you measure the value of a string of ideas coming out of a marketing department?

If knowledge worker A works for ten hours and knowledge worker B for eight hours, most people will assume that B has the easier job, not that he is more efficient at it. "Alas," writes Mr Davenport, "there is no Frederick Taylor equivalent for knowledge work. As a result we lack measures, methods and rules of thumb for improvement. Exactly how to improve knowledge-work productivity...is one of the most important economic issues of our time."

One way, he suggests, might be to examine how different workers use knowledge; to see which technologies best gather and disseminate the information that knowledge workers need; and to find the workspace that is best suited to people who are highly mobile and need to concentrate a lot.



The sort of technologies he has in mind are the sophisticated online directories that companies have developed to help employees identify expertise and knowledge held by others within the organisation. Examples include Hewlett-Packard's Connex, Motorola's Compass and IBM's Blue Pages Plus. To some extent the effectiveness of these systems can be measured in a Taylor-like way. How many human connections did they enable to take place during a certain period? How valuable do users find them, on a scale of one to ten?

Companies now are investing huge sums in such systems of "knowledge management", which include their intranets and their internal databases. One company describes its intranet as "a vibrating current of what is going on in the business". The challenge is to ensure that employees can plug into this vibrating current as and when they need it.

There are three broad approaches to knowledge management. One is to create a system where all information goes to everybody, which is hugely inefficient; the second tells people what others think they need to know, which may not match their real needs; and the third enables them to find for themselves whatever they want to know. Companies like to say that they aim for the third approach, but they do not always find it easy.

In the end, though, do knowledge workers not always contribute something that is unmeasurable? Yves Morieux, a

consultant in the Paris office of the Boston Consulting Group, certainly thinks so. “The most valuable human mechanisms are not measurable,” he maintains. As an example, he points to the fact that Olympic relay races are often won by teams whose members do not have the fastest aggregate times. When Mr Morieux talked to members of a French Olympic medal-winning women's relay team, he was told that at some point you have to decide whether to run your guts out and literally not be able to see straight when you pass the baton; or whether to hold something back to make a better baton-change and enable your team-mate to run a faster time. The value of this sort of decision-making —each individual's contribution to the team—is, he says, beyond measure.

Mr Morieux concludes that companies should concentrate on designing the processes that knowledge workers carry out, rather than measuring their performance. The key to the success of Ryanair and other low-cost airlines, he says, lies in the way they think about combining processes. Ryanair's cabin crews also do the cleaning inside the aircraft, so if they make a bad job of it they have to face complaints from passengers. In more traditional airlines the cleaners never see the passengers.

Business, says Mr Morieux, is about the sort of trade-offs that Ryanair stewards are making all the time—between punctuality and cleanliness, between service and speed. In the organisation of the future, he says, the main tasks of managers will be to judge what are the most important trade-offs for their particular business; then to decide who is best placed to make decisions about those trade-offs; and finally to delegate responsibilities accordingly.

So what is required to build and maintain the kind of “new organisation” in which knowledge workers will thrive? The three words that most commonly crop up in answers to this question are leadership, talent and culture. To look at the shelves of business books on leadership, the visitor from Mars might imagine this was something that the business community on Earth had only just discovered. But current interest in the subject has been greatly stimulated by the spread of the “disaggregated” organisation: with more responsibility handed down to the workforce at large, many more people than before are having to exercise leadership. The market for books on the subject has grown by leaps and bounds.

The leaders who feature as role models for businessmen these days have changed as well. Few people are looking for lessons in modern leadership from Alfred Sloan, the legendary architect of the once-great General Motors, or Thomas Watson, creator of the first great incarnation of IBM, or indeed Bill Gates, founder of Microsoft. Instead, the most popular figures from history are probably Alexander the Great and Ernest Shackleton.

Alexander is a perennial favourite, given a boost in this era of globalisation by his claim to be the first leader with a truly global vision, the first great bridge between East and West (never mind that one contemporary described him as “murderous and melancholy mad”, and that he died of alcohol poisoning at 32).

Shackleton failed to achieve the goals of his polar expeditions, but saved all his men by beating a retreat that required great courage. His story strikes a chord with members of the new organisation, where looking after your team is valued more highly than carrying on regardless in search of some big strategic goal.

Which way up?

The flattening of the organisation has had at least one unexpected consequence. With fewer rungs on the ladder, there is now less opportunity to make visible progress to the top: promotion within the company has become rarer. Some people worry that this will leave a dearth of people with enough experience needed to run an organisation. To counter this, GE and Procter & Gamble have developed a cadre of three vice-chairmen with broad areas of responsibility who are the heirs apparent—CEOs in training.

Young managers are frustrated by having fewer opportunities for promotion; in a recent poll of British managers, 38% said that their company's flatter structure was a barrier to their career. The temptation is to move to another company that can offer an intermediate rung on the ladder.

One of the main challenges for leaders of the new organisation is to hold on to the knowledge workers who are essential to its operation. Some companies have been re-examining the way they reward knowledge workers. Booz Allen Hamilton's Gary Neilson says that for talented people in western companies today, financial incentives matter less than non-financial ones—things such as esteem, a challenging and varied job, and the chance to work in teams. Knowledge workers get a lot more out of corporate life than a pay cheque at the end of the month. For many it is an important channel for meeting new people at a time when traditional organisations which served that purpose—such as churches and clubs—are in decline.

According to Jay Lorsch, at Harvard Business School, affluent societies often assume, wrongly, that workers are motivated only by money. Bostonians were astonished late last year when Theo Epstein, manager of the hugely successful Boston Red Sox baseball team, walked away from a multi-million dollar contract at the age of 31, saying

that he was looking for a different kind of fulfilment.

Henry Ford is credited with a flash of business genius when he doubled the pay rate of manual workers on his assembly lines in 1914. By putting the cars they were making within their financial reach, the story goes, he sharply increased the market for his Model Ts. But there may have been a more prosaic reason. Work on the assembly line was so boring that Ford had to provide his employees with large financial incentives to stop them moving back to more traditional manufacturers, where they were responsible for a much larger part of each vehicle.

Knowledge workers may not be tempted by such bribes. Money remains important, but it is being used to achieve different objectives. At IBM, the emphasis in the annual bonus schemes has shifted away from the performance of the employee's individual unit and towards that of the company as a whole. Linda Sanford, a senior vice-president at IBM, says it has not made a huge difference to the amounts paid out, but it has sent a signal that the company wants people to work together.

At Toyota, most of a manager's bonus is linked to the performance of the business in the whole of his region, and only a small amount to his individual performance. BP strips out changes in the price of oil and foreign exchange from its profit-sharing scheme because they are outside its employees' control.

Some companies have discovered that one way they can reduce the loss of talent is by keeping their doors open. Traditionally, once employees had left they were not welcomed back. A senior executive leaving a blue-chip investment bank, say, would never return. Today the banks' attitudes are different. McKinsey too has begun to re-recruit former employees. David Thomas, a professor of business administration at Harvard Business School, explains that companies need to accept that they may not be able to excite all the talented people on their payroll all the time. So let them go, he says, and try to entice them back later.

Keeping the doors open will also help women enter the higher echelons of management, where they have been persistently under-represented. They are far more likely than men to leave an employer in mid-career, if only to have children. Yet few end up returning to their former employers, and those that do rarely return on the same terms as they left. One survey in America last year found that women re-entering the workforce after an absence of three years or more suffered an average reduction in salary of 37%.

But re-entry problems are not encountered only by women. On the beaches of California, a lot of male business-school graduates walk around with surfboards under their arms. They have worked for a time, earned some money and decided to do something different. One day they may want to return to work. Companies that are not prepared to welcome such people back will lose out.

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Inculcating culture

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The Toyota way

IN AN organisation whose employees are self-motivating and largely self-directing, the compass that steers them in the way the organisation wants them to go is its culture. Toyota has 580 different companies around the world, 51 factories outside Japan, and sells cars in more than 170 countries. What holds these operations together and makes them part of a single entity, says Takis Athanasopoulos, the head of its European operations, is the company's strong corporate culture.

“The Toyota Way”, which embodies the Japanese carmaker's culture, has five distinct elements:

•*Kaizen*, the well-known Japanese process of continuous improvement. *Kaizen* is more a frame of mind than a business process. Toyota employees come to work each day determined to become a little better at whatever it is they are doing than they were the day before.

•*Genchi genbutsu* (GG), which roughly translated means “go to the source”. Find the facts and do not rely on hearsay, because it is easier to build consensus around arguments that are well supported. And also go to the source of the problem. Mr Athanasopoulos says that western companies spend too little time defining what business problem they are facing, and too much time coming up with solutions. GG puts the emphasis the other way round.

•Challenge. This is reminiscent of the Chinese proverb, “May you live in interesting times.” Toyota employees are encouraged to see problems not as something undesirable, but to view them positively as a way to help them to improve their performance further.

•Teamwork. This means putting the company's interests before those of the individual, and sharing knowledge with others in the team. Much of this does not come naturally, and Toyota devotes a lot of time and money to on-the-job training.

•Respect for other people, not just as people but also for their skills and the special knowledge that derives from their particular position in the company. Toyota believes that if two people always agree, one of them is superfluous. Different opinions must be expressed, but in a respectful way.

Once these values are inculcated into a worker, they guide decision-making throughout the day. There is no need to refer matters up the silo to ask what to do. Everyone knows what solution should be adopted, so decision-making is dramatically speeded up.

Japanese colleagues who know the culture well, says Mr Athanasopoulos, reach a point of “emotional fortitude” where their behaviour is entirely consistent with the organisation's culture and beliefs. In the West, where individual interests tend to be put before those of any group, it is more difficult for employees to reach this state. It may be something that will give the “new organisation” in Japan an intrinsic advantage over its incarnations elsewhere.

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Teaming with bright ideas

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Better ways of working together

COMPANIES are eager these days to emphasise that they are organised around teams. A recent series of advertisements for Microsoft featured teams of employees from the giant software company getting excited about the various projects on which they were working together.

Headhunters are increasingly being asked to assemble teams of top executives, not merely to find a single high-performing CEO. And the bosses themselves are expected to be good at putting together teams. David Nadler, the founder and head of Mercer Delta, has recently published a book called “Building Better Boards” arguing that it is time for the corporate board to reinvent itself “and become a high-performing team offering real value to the company”.

The speed and efficiency with which effective teams can be brought together to resolve problems is crucial to success in the modern organisation. In a recent *Harvard Business Review*, Philip Evans and Bob Wolf, who work for the Boston Consulting Group, explained how teamwork within Linux, the open-source software “community”, managed to build a barrage to protect the system against a virus that had breached a vulnerable spot: “Despite the need for the highest security, a group of some 20 people, scarcely any of whom had ever met, employed by a dozen different companies, living in as many time zones and straying far from their job descriptions, accomplished in about 29 hours what might have taken colleagues in adjacent cubicles weeks or months.”

The authors argue that Linux was more successful at resolving the problem than its more conventionally structured rival Microsoft would have been. The article holds up the Linux crowd as the “virtuoso practitioners of new work principles that produce energised teams and lower costs.”

But it is not just geeks in the software industry who have learnt to work in this way. Messrs Evans and Wolf say that the management methods of Toyota, the company that invented “lean manufacturing” (the remorseless elimination of waste) resemble, “in a number of their fundamentals, the workings of the Linux community”. One stroke of genius of the so-called Toyota Production System was to apply the principles of lean manufacturing to inventory. What could be more wasteful than having shelves piled high with supplies that were not going to be used for weeks or months?

This gave rise to the famous “just-in-time” method of stock control. Toyota realised that the best way to make this system work was to allow the workers on the factory floor to control the flow of supplies, because they had the information that would keep stocks at their lowest. This forced Toyota to decentralise decision-making and, unlike most Japanese companies, empower its shop-floor workers.

In recent years Japanese companies have swung from being undisputed stars of management practice to being mere organisational mortals. The controls and formal hierarchies that made them such formidable production machines in the 1980s are no longer seen as a big competitive advantage; indeed rather the opposite.

However, Messrs Evans and Wolf argue that Toyota has now moved beyond lean. “In the Linux and Toyota communities,” they say, “leading is not treated as a discipline distinct from doing. Rather, the authority of leaders derives from their proficiency as practitioners.”

In its latest annual report, Toyota describes a significant new feature of its management system: “Senior managing directors do not focus exclusively on management. They also serve as the highest authorities in the specific operational functions.” In other words, specialists have become leaders. This system, says the company, “helps closely co-ordinate decision-making with actual operations”. It is no coincidence that Toyota's new president was previously the head of its supply-chain management.

Clusters, mules and brokers

To see how they might make teams work better, companies have begun to look at the informal networks that employees create outside their organisation's formal structure. Mapping of such networks shows that most people stick together in clusters of eight to ten like-minded souls, a group with whom they undertake the vast majority of their communications and with whom they feel “safe”.

There is, however, a certain sort of individual who moves across different clusters. He or she is likely to take part in lots of activities and associate with people from other departments. He is not necessarily the most charismatic person in a group, but by acting as a “knowledge mule”—someone who carries ideas from one corporate silo to another and thereby sparks off new ideas—he is a key figure.

Brian Uzzi, a sociologist at Kellogg business school, part of Northwestern University just outside Chicago, has looked at ways in which companies can make use of such mules, whom he calls “brokers”. Some law firms, for example, try to identify them and reward them differently, because their value lies in bringing ideas together within the firm, not in bagging new clients, which in the legal profession is the more usual yardstick for rewards. Mr Uzzi thinks that companies should try to identify brokers and make it their business to recruit them.

The more that workers interact with each other, the more likely they are to solve the problems of complexity that are a feature of modern organisations. “The value of interactions is rising”, says the Boston Consulting Group's Mr Morieux, “because their generative function [meaning their ability to generate new ideas] has become the solution to increasingly challenging organisational problems.” MBWA—Management by Walking Around, a style championed by Bill Hewlett and David Packard in the 1960s and 1970s as they built up their company, had the boss leaving the rarefied atmosphere of his executive suite and wandering around to see what the troops were up to. The modern-day version of this is MBTA—Management by Talking Around.

It also matters how you talk. Face-to-face or over the phone? By voicemail or by texting? The rapid development of telecommunications has opened up all sorts of new options, yet little research has been done into the relative effectiveness of new ways of communicating.

It seems to make a difference whether a communication is synchronous (eg, the telephone, where you get an immediate answer to your question) or asynchronous (eg, e-mail, where you send a message and then wait for the answer). Research indicates that a complicated sales pitch is less likely to succeed using asynchronous methods. If you want to escape from a predatory salesman, ask him to make his pitch in an e-mail.

The Boston Consulting Group's Mr Evans says that face-to-face contact is valuable for establishing trust between people, but once that has been done, it does not need to be repeated very often. People will happily deal at a distance with parties they have come to trust. Mr Evans also points to the growing sophistication of virtual environments (as seen in electronic games such as “Second Life”, in which players interact online with as many as 70,000 other players around the world). He believes these will cause people to rethink what they can do together without actually getting together physically.

The minutiae of meetings

For the moment, despite the growth of virtual alternatives, the most efficient way to get decisions made is often to sit people round a table for a discussion. Indeed, the virtual alternatives to such meetings are becoming increasingly good at recreating that environment. The latest videoconferencing equipment gives participants the

impression that they are facing a bunch of people sitting round a table.

Businessmen still go to great trouble and expense to get together with other businessmen and talk. Meetings may stick more closely to the agenda than they used to, and waste a little less time, but the formal business meeting is far from extinct. Indeed, as decision-making has been spread more widely within business organisations, and as more people have become involved in it, the number of business meetings has probably increased.

Some companies are attempting to get more value out of this plethora of meetings. Victoria Medvec at Kellogg business school says that when people sit down together, there is a tendency to seek confirmation of what everyone already knows. To avoid this, she suggests, participants should do two things before they even start opening their mouths. They should write down what they think about particular items on the agenda, and they should rate the strength of their views on a scale of, say, one to ten. That way, she says, participants will remember what they thought before their views were influenced by others.

The emerging “new organisation” pays more attention than did its predecessors to the environment in which people work. Physical space matters, if only to the quality of communication. Some companies are reinventing the “skunkworks”, groups of people who work on a project outside the company's normal rules (and outside its normal places of work) to help them come up with extraordinary results. IBM famously used this method in 1980 to invent its personal computer.

The skunkworks concept fell into disrepute when it was seen as just another cost centre, and one with attitude at that. Now it is being revived, but in a different guise. Much of Motorola's Razr mobile phone, currently a big market hit, was developed in a new laboratory that the company has set up in downtown Chicago, 50 miles (80km) from its main R&D facility in suburban Illinois. The building and the design of the workspace are very different from Motorola's main offices, with lots of bright colours and no dividing walls.

In this type of skunkworks, geniuses are not just left to breathe pure intellectual air, as they often were in previous incarnations; they are also constantly brought into contact with designers, marketing people, production managers and accountants. The idea is not that they emerge at the end of the day with something that makes their competitors say “wow”. It is that they come out with something that makes their competitors' customers say “wow”.

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Big and no longer blue

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A totally new, improved IBM

IBM has been an early adopter of many of the features of the new organisation. As Linda Sanford, a senior vice-president and one of the highest-ranking women in the company, puts it, “you have to have an organisation that senses change and by itself identifies a working team that can go after the opportunities.” To help create such an environment, the chairman and chief executive, Sam Palmisano, in mid-2003 decided that the company needed to rethink and restate its values. When employees are released from central control, the strongest glue holding them together is the set of values embraced by the organisation they work for.

Following a 72-hour online real-time chat session with its employees, IBM came up with its three values for the 21st century: “dedication to every client's success”; “innovation that matters, for our company and for the world”; and “trust and personal responsibility in all relationships”. It may seem banal, but there is common ground here with many other modern firms. IBM has also opened an online suggestions box called “Think Place” where ideas are logged for all to see and to improve upon. Of the first 4,500 to appear, 300 have already been adopted.

The company has devoted considerable resources to redesigning its intranet, its internal online data and its communications system. Like others, it is trying to change the system from being a mere means of distributing messages to becoming a lure that brings together seekers of knowledge and collaborators. Identifying employees with particular expertise within the company has become easier.

“We have to let go of the old command-and-control structure if we're going to grow,” says Ms Sanford. In a book published last month, “Let Go to Grow”, she argues that instead “businesses must adopt a culture of collaboration—both within their four walls and outside them.” The good news is that the technology to do that is now available.

An internal account of how the company resolved a technical problem in the wake of Hurricane Katrina shows how such collaboration can work: “Using our Blue Pages Plus expertise locator on the corporate intranet, we found the right people within the space of an hour or two, and had a wiki [a web page that can be edited by anyone with access] up and running. Using the wiki as a virtual meeting room, a team of IBMers from the US, Germany and the UK were able to offer a solution to the problem in the space of just a few days.” It all sounds very 21st century. But it will work only if the right incentives are in place to persuade people to work in unconventional ways.

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Partners in wealth

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The ins and outs of collaboration

THE new organisation contains a mass of contradictions. Charles Knight, Emerson's long-time boss, boasts that his company combines consistency with fundamental change. Parts of Motorola are centralised and parts are not, and those parts change over time. The company's skunkworks, for example, are decentralised to encourage innovation, but its accountants are centralised. “We don't want highly innovative accountants,” says Motorola's Mr Canavan.

In a paper entitled “The Strategic Enterprise: Rethinking the Design of Complex Organisations”, Mercer Delta describes its vision of the organisational architecture of the future, made up of a number of strategically aligned businesses “linked closely where there are opportunities to create value by leveraging shared capabilities, but only loosely where the greater value lies in differentiated focus”. In other words, close and loose relationships will coexist within the same organisation.

In the traditional organisational structure, units were either within the organisation and, as Mercer Delta's David Nadler puts it, “densely connected”, or they were outside the organisation and not connected at all. Transactions with external suppliers were at arm's length. By contrast, companies today cohabit with a vast number of joint-ventures and strategic alliances, some more and some less connected. The line between what is inside and what is outside the corporation, once so clear, has become blurred.

One of the most contentious of these new relationships is outsourcing—the handing over to others of what were once considered to be core functions of the company. First to be transferred to more efficient providers were companies' manufacturing operations. Firms such as Nike have stretched this idea to such an extent that some of them now make nothing: all Nike's shoes, for instance, are manufactured by subcontractors. Nike employs few people directly. Such companies have become the orchestrators of a brand. Their baton has only limited control over the musicians who play for them, but that does not prevent them from producing great music (or shoes).

Even such a quintessential manufacturer as Procter & Gamble has joined this bandwagon. “Our core capability is to develop and commercialise,” its chief executive, A.G. Lafley, has said. “We concluded in a lot of areas that manufacturing isn't [a core capability]. Therefore I let the businesses go do more outsourcing.”

The enthusiasm for outsourcing has recently spread to service jobs such as accounts and IT. One of the fastest-growing areas now is human resources (HR). Kennedy Information, a firm of analysts, estimates that the global HR outsourcing market will grow by 25% a year for the next few years. In November 2005, DuPont, a multinational chemicals company, outsourced its HR services, such as workforce planning and deployment, labour relations and performance management, to Convergys Corporation, a firm based in Cincinnati. The 13-year contract covers 60,000 employees and 100,000 pensioners in 70 countries and is worth $1.1 billion.

But outsourcing is a fluid business. Work that has been handed over to others is sometimes “insourced” back, and not necessarily because it was being done badly outside. Some banks, for example, are bringing the processing of

payments back in-house because they have realised that the data they have been handing over to others can become a platform for new business. Software programs that mine data in novel ways can throw up ideas for new products and markets. Over the next few years companies may well come to reassess the value of their HR operations and decide that workforce planning and performance management have become sources of competitive advantage over which they wish to retain control.

The relationships within the new organisation, with their varying degrees of connectedness, can be tricky. Along with greater dependency among businesses, they create new areas of uncertainty. How does a bank protect itself from the risk that employees of a company to which it outsources might steal its customers'PIN numbers? And what happens if the partner in a joint-venture goes bankrupt?

Howard Kunreuther, a business professor at the Wharton School in Philadelphia, argues that this interdependency “is probably the most important issue to start thinking about with regard to risk”. Ravi Aron, another Wharton professor, says that companies need “an extended organisation form”, with one shape for the outsourced “market” operations, and another for the in-house “hierarchy”. The focal point of this extended organisation is a “programme office” where the company and its outsourcers collaborate on matters of mutual interest, such as quality control and performance. According to Jon Watts, a consultant with Booz Allen Hamilton, “it's got to the point where the outsourcing provider and the client company may form alliances and take financial stakes in one another to make sure their interests are aligned.”

Up in the air

A good example of how corporate relationships have changed in recent years is Boeing. The process for developing and manufacturing the aircraft-maker's current 787 model has been totally different from the one used for earlier models. Before the 787, Boeing did all the engineering design work itself. The main reason to change, says Mike Bair, head of the 787 development team, was that the company realised it had to trawl the world and find the best suppliers in order to compete with its main rival in the market for commercial aircraft, the increasingly successful Airbus.

Airbus, a joint European venture involving French, German, British and Spanish partners, started from scratch. Almost by accident it stumbled on an organisational architecture that, along with generous subsidies, helped it overtake the giant of the business in less than two decades.

These days, Boeing is organising itself more like Airbus. It scoured the globe for new partners and found some in Europe, some in Japan and some not far from its home base in the United States. Whereas with the 777 aircraft the company worked with 500-700 suppliers, for the 787 it has chosen just under 100 “partners”.

The difference is not just in the numbers, but in the relationship. Suppliers provide what they are asked for; partners share responsibility for a project. For over six months in 2005, teams of people from the various 787 partners met at Boeing's base in Everett, north of Seattle, to work together on the configuration of the plane—something that until then Boeing had always done by itself. Now the partners are back at their own bases, responsible for all aspects of their piece of the puzzle. The partners are building their own production facilities for their bits of the aircraft. The first flight is scheduled for 2007, and the 787 is due to come into service in 2008. As Mr Bair says, “it puts a high premium on the choice of partners in the first place.”

It also puts a high premium on the management of that network of partners. Boeing holds a partners' “council meeting” every six weeks, and has set up a network to facilitate global collaboration which makes it possible for designers all over the world to work on the same up-to-the-minute database.

The company is also putting great faith in videoconferencing and has set up high-bandwidth facilities that are in constant use. People come into their offices in the middle of the night to have virtual meetings with colleagues in different time zones. Technically, the 787 will be an American plane; but in reality it will be a global one.

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The X and Y factors

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What goes around, comes around

ALMOST since the day it began, the dominant academic discipline behind the “science” of management has been engineering. When Oxford University first allowed management to be taught as an undergraduate subject (as recently as the late 1970s), it was introduced as a combined “engineering and management” degree.

Some of the most famous management gurus, notably Michael Porter, Michael Hammer and Tom Peters, trained as engineers first. Many of the most influential business leaders were also engineers, including Alfred Sloan, who built General Motors, and Jack Welch of GE. Their training taught them to divide things up into small pieces, make each piece better and then put them all together again. It was a bit like Legoland.

Management science's founding father was yet another engineer: Frederick Winslow Taylor, who wandered round factories with a stopwatch and a clipboard to measure workers' productivity. It was the job of the managers, he told them, to improve that productivity by refining the processes the workers had to perform. In Taylor's world, improvement was defined by time and motion.

Just occasionally, different academic disciplines would raise their heads and suggest that they, too, might have something to add to the thinking on organisational improvement. The economist Ronald Coase, for instance, argued in the 1930s that firms existed to reduce the transaction costs involved in doing things—in particular, the cost of finding business partners, making contracts with them and monitoring the contracts thereafter.

Faster, cheaper telecommunications and the emergence of the internet have dramatically reduced such transaction costs. The advantages of a firm over a marketplace full of independent contractors have been eroded. In consequence, firms have outsourced many of their operations into marketplaces, or are trying to foster internal, in-house marketplaces.

Psychology too has had its moments. Elton Mayo's experiments at the Western Electric Company's Hawthorne plant near Chicago in the late 1920s became a landmark, demonstrating that there was an aspect to productivity that transcended time and motion. When the lights in the factory being monitored were made brighter, productivity improved, as you might expect. But when the lights were made dimmer, productivity unexpectedly improved further. As it turned out, it was not the dimming or brightening of the lights that had an effect, but the attention that the workers were getting.

Beyond engineering

In the 1990s engineering enjoyed a renaissance, in the guise of Business Process Re-engineering (BPR), the dominant management idea of that decade. BPR involved reorganising the company around processes such as purchasing, marketing and distribution, which cut across the traditional corporate silos based on products and geography. This involved using different building blocks, but it still treated the company as a series of pieces to be taken apart, improved and put together again like Lego.

The “new organisation” breaks free of this engineering heritage. In “Results”, a recent book by two Booz Allen Hamilton consultants, Gary Neilson and Bruce Pasternak, the authors talk about “the DNA of living organisations”. Corporate DNA, they suggest, consists of “four basic building blocks: decision rights; information; motivators; and structure”. These combine in different ways to make more than the sum of their parts, expressing distinct identities or personalities. McKinsey's Lowell Bryan also talks about “the personality of the firm”.

This switch, from Lego to DNA, echoes one of the best-known classifications of corporate culture ever made. In “The Human Side of Enterprise”, originally published in 1960, Douglas McGregor, a Harvard academic, divided management styles into Theory X and Theory Y. Theory X was the classic command-and-control type of management, the authoritarian style which (McGregor wrote) “reflects an underlying belief that management must counteract an inherent human tendency to avoid work.” This is the world that Frederick Taylor observed, and the world that organisation man was designed for.

Theory Y is the antithesis of X. It “assumes that people will exercise self-direction and self-control in the achievement of organisational objectives to the degree that they are committed to those objectives”. Theory X is bent on devising the right sticks with which to prod work-shy labour; Theory Y looks for the carrots that will induce them to stay.

McGregor's dichotomy has been hugely influential in management thinking ever since his death in 1964. The new organisation lies firmly at the Theory Y end of his spectrum. It challenges employees, in his words, “to innovate, to discover new ways of organising and directing human effort, even though we recognise that the perfect organisation, like the perfect vacuum, is practically out of reach.”

McGregor himself came to believe that neither management style in its pure form could work successfully. Firms would find a balance between the two that would shift over time to fit new circumstances. But the new organisation is beginning to prove him wrong. Companies are coming to realise that knowledge workers, who have been identified as the creators of future wealth, thrive only under Theory Y. Theory X is becoming extinct—just like organisation man himself.

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The public relations industry

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As advertising struggles, PR steps into the breach

“NEWS is what someone wants to suppress. Everything else is advertising,” said Reuven Frank, a former head of NBC news. So what sort of business is public relations (PR), which spends half its time huffing about bad news; and the rest puffing politicians, companies and celebrities?

The answer is that, for business, PR is an increasingly vital marketing tool—especially as traditional forms of advertising struggle to catch consumers' attention. The goal of PR is usually to secure positive coverage in the media, and the well-worn tactics include calling a press conference, pitching stories directly to journalists, arranging eye-catching events, setting up interviews and handing out free samples. But as PR profits from advertising's difficulties, it is taking up a host of new stratagems—and seeking to move up the corporate pecking order.

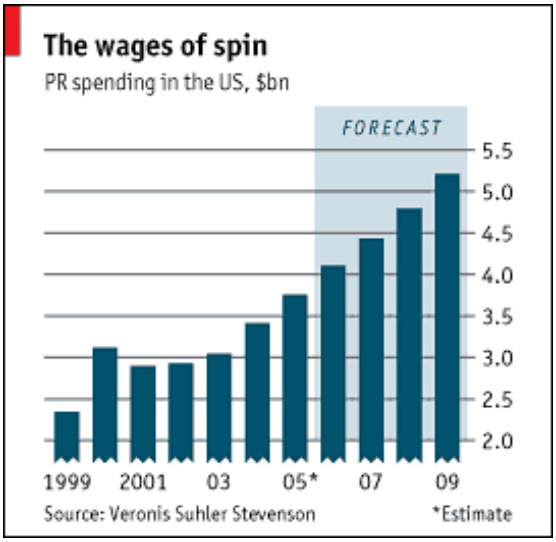
Some journalists regard PR people as a nuisance, or worse. Even so, PR is surprisingly effective, at least according to a recent study by Procter & Gamble, the world's biggest consumer-products group. P&G is a firm that marketers pay a lot of attention to, not least because of its advertising budget of some $4 billion. It has always been at the cutting-edge of marketing—P&G is credited with inventing the television soap opera as a new way to sell goods. But with fewer people watching television and the circulation of many papers and magazines declining, the firm has become pickier about where it spends its advertising budget. Increasingly, it wants a measurable return on investment from its campaigns.

In a recent internal study, P&G concluded that the return was often better from a PR campaign than from traditional forms of advertising, according to Hans Bender, the firm's manager of external relations. One reason is that in comparison with many other types of marketing, PR is cheap. In P&G's case, it can represent as little as 1% of a brand's marketing budget. That proportion could now rise, says Mr Bender, although he hastens to add that other forms of advertising and marketing would remain important for the company.

If P&G starts to spend more on PR campaigns it will confirm a trend. Spending on PR in America has been growing strongly (see chart) and reached some $3.7 billion last year, according to Veronis Suhler Stevenson, a New York investment bank that specialises in media. It forecasts PR spending will grow by almost 9% a year. This is faster than the overall market for advertising and marketing, now worth a colossal $475 billion and growing at 6.7% a year.

Of course, not all PR people are selling products or services. Indeed,

marketing PR—or “brand communications” as it is sometimes called—is still considered by some in the industry as something of a Cinderella business. A recent study in Britain by the Centre for Economics and Business Research found the PR industry there employs 48,000 people. More than 80% were working “in-house”, for companies or other organisations. Just over half of Britain's in-house PRs work for the public sector, health organisations and charities. These organisations are also the biggest users of PR consultancies.



Many of the big PR firms have been consolidated into the giant groups that now dominate the advertising industry. Two of these are American: Interpublic owns GolinHarris and Weber Shandwick, and Omnicom owns Fleishman-Hillard and Ketchum. Britain's WPP owns Hill & Knowlton and Burson-Marsteller. The groups also own a range of specialised agencies. For instance, WPP's Finsbury concentrates on corporate and financial PR—and has just gained publicity by announcing that it is taking on Tony Blair's son, Euan, as an intern. Omnicom's Clark & Weinstock does reputation and crisis management, and Interpublic's PMK/HBH looks after the entertainment business, with celebrity clients such as Nicole Kidman, Russell Crowe and Jennifer Aniston.

Then there are the independent PR firms, the largest of which is family-owned Edelman. Richard Edelman, the company's president and chief executive, says that Edelman's own studies show the most credible form of communication now comes from “a person like yourself”, which suggests that PR firms have new opportunities to influence peer groups.

Edelman, for instance, recently worked on drumming up interest amongst hard-core computer-gamers ahead of the launch of Microsoft's new Xbox games console. It also worked for a group of former executives who last year succeeded in ousting Philip Purcell as chief executive of Morgan Stanley. One of the things the PR firm did was to set up a website where employees of the Wall Street investment bank could have their say in the controversy. Such work is very different from classic public relations. “Companies can try to serve up a tight, straight message through the media by issuing a one-way press release, but that's as flawed right now as a 15 or 30-second TV ad,” says Pam Talbot, Edelman's chief in America.

The fragmentation of media has seen an explosion in the number of ways people seek news and entertainment, with many turning to websites, cable TV, satellite radio and podcasts. Yet a consequence of the proliferation of media is that original content becomes even more sought after. Hence crisply written or well-produced PR material can more easily get an airing. Media commentators have noted how PR material is now being published by some local newspapers virtually unedited and unchecked. Some branches of journalism have come to depend on a drip-feed of information and products from the PR industry. Journalists focusing on electronics, fashion, travel, beauty and food have a huge appetite for free samples. Gossip about celebrities is also largely mediated by the PR industry.

Never shy about accentuating the positive, the PR industry might be expected to be trumpeting its rise. And there is indeed some triumphalism (and spin) around. Al and Laura Ries, a father and daughter team of marketing consultants, have written a book entitled “The Fall of Advertising & the Rise of PR”. “PR has credibility,” they assert: “Advertising does not.” Their advice is that a marketing campaign should start with publicity and shift to advertising only after the PR objectives have been achieved. Some PR firms see an opportunity to move up their clients' hierarchy—becoming not just service providers, but also purveyors of strategic advice to senior management.

But even within the industry, there are sceptics. Dorothy Crenshaw, president of Stanton Crenshaw, an independent PR firm based in New York, says that many of her colleagues are suffering from “consultant envy”—but that PR remains a very inexact science. There are also limits to the miracles it can be expected to achieve. She claims to have turned down a $1m commission from a client desperate to boost his business-to-business website in the midst of the dotcom boom because he had nothing much to tell the world. Sometimes a PR firm can indeed shape or create a buzz about a product, but not always. For PR to work, she says, “you have to have a legitimate story.”

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Newspapers

Extra, extra

Jan 19th 2006
From The Economist print edition

Desperate times bring desperate measures

ptpx

The DVD wars

IN A letter about pay-rises to staff at the *Sun* last year, Britain's biggest-selling newspaper, Rebekah Wade, its editor, remarked that in future the paper's success would probably depend more on free CDs and DVDs than on its journalists. British newspapers are frenziedly giving things away, and in Germany, France, Italy, Poland and throughout Latin America papers are also increasingly relying on freebies to try to attract new readers. In Britain the circulation of national newspapers fell by 3% in 2005, following a 2% decline in 2004. The same pattern of falling circulation is being repeated across Europe and the United States. So are all the free gifts a sign of desperation from newspapers, or an entirely sensible new marketing strategy?

Ideally, a giveaway attracts brand-new readers who keep on buying the paper. Newspapers particularly hope that CDs and DVDs will appeal to the young—who are increasingly getting their news online. For a paper selling copies in the hundreds of thousands each day, it costs about $1m-1.5m to give a DVD away at the weekend, and less for a CD. A good film can push a day's circulation up by 20% or more. But the strategy covers its costs only if new readers stay during the rest of the week, and the paper gains a larger base for its advertising sales.

Plenty of newspapers still regard giveaways as beneath their dignity. Quality papers in America, for instance, do not go in for them (so far). It looks much more respectable, says Michael Smith, of the media department of Northwestern University, if freebies dovetail neatly with a newspaper's brand. In Latin America, he says, several papers, such as *La Nueva Provincia* in Argentina, have given CD collections of regional folk music. In Britain this week the *Financial Times* (which owns a 50% stake in *The Economist*) gave away the first of a weekly series of condensed editions of business books.

Elsewhere, newspapers have managed to charge more for editions that come with an extra something. Italy's *La Repubblica* is charging a few euros more on the days when it encloses one of a series of books, and *Le Figaro* and *Le Monde* in France also lift their price when they carry DVDs or other giveaways.

Some newspaper bosses take an entirely cynical view of the practice. Rupert Murdoch, owner of the *Sun* and the *Times*, said last November that he dislikes it because “people grab the paper, tear the DVD off and throw away the paper”. Despite his views, points out a rival newspaper executive, his titles in Britain have given away far more freebies than their competitors have, and are still handing them out. In fact, many newspapers have little choice but to give away things, because everyone else is at it. “It all started with some integrity,” says Marc Sands, director of marketing at the *Guardian,* “but now people are doing anything to get a spike in circulation.” Yes indeed: on January 14th, the largest headline on the front page of the *Guardian* screamed “Free DVD”.

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Oil

Take your partners

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From The Economist print edition

China, India and the oil market

THE global scramble by China and India for oil assets abroad started to worry western oil majors last year. Egged on by governments concerned about energy security, once-irrelevant Asian energy firms gobbled up oil and gas everywhere from Ecuador to Canada to Kazakhstan. China's CNOOC even made an audacious (although ultimately unsuccessful) $18.5 billion bid for America's Unocal. But the setback has not dented CNOOC's ambitions. The company has just announced a successful $2.25 billion deal for oil and gas assets in Nigeria. There are market rumours that the same Chinese firm is now looking to snap up Nations Energy, a Canadian firm with assets in Central Asia, for a further $2 billion. The new king of Saudi Arabia has just announced that his first trip abroad will be to China and India.

Western majors, which are already finding it hard to replace their oil reserves, see the emergence of new Asian rivals as a sign of trouble ahead. And the past few weeks have raised the spectre of a force even more threatening than China and India competing to buy assets: the insecure giants working hand in hand.

Given the historical animosities between the two countries, that may seem unlikely. But Mani Shankar Aiyar, India's petroleum minister, signed a series of energy co-operation agreements during a visit to China this month. Mr Aiyar proclaims that, from now on, the two countries will see each other less as strategic competitors than as strategic partners.

The Indians have an interest in working with Chinese oil firms because, in recent years, they have been consistently bested by their richer neighbour. Over the past couple of years, Chinese companies edged out Indian ones in Ecuador, Kazakhstan, Angola and Indonesia. But why would the Chinese bother to co-operate with the Indians? Geopolitical machinations offer one possible reason. America has recently cosied up to India, offering it nuclear technology and other carrots. It may suit China to offer the Indians some rival attractions, by jointly bidding for assets in Iran, Myanmar and other countries that are out of favour with America.

Co-operation would also make some financial sense. During last year's bidding for PetroKazakhstan, a Canadian outfit with lucrative oil assets in Central Asia, the Chinese paid a premium of perhaps $500m to see off a rival Indian bid. And there is evidence that co-operation is more than just talk. As if timed to silence critics before the ministerial love-in, India's ONGC Videsh and China's CNPC announced last month that a joint bid had secured a stake in an oil field in Syria—not exactly America's favourite ally.

But while the two countries will work together when it suits them, they will also continue to pursue their energy interests separately as well. The Chinese have their African and Central Asian deals. And India's ONGC has just agreed to work closely with Shell to develop and produce oil across the world. In the new oil world there will be no clear dividing line between rivals and partners.

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Telecoms

The teachings of the Virgin

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Why the telecoms industry is gripped by dealmaking frenzy

THE on-again, off-again courtship of Virgin Mobile, a British mobile operator, by NTL, the country's dominant cable firm, resumed this week when NTL raised its initial offer of £871m ($1.5 billion), made last month, to £961m. Sir Richard Branson, who owns 71% of Virgin Mobile, wants the deal to be pushed through. There are still plenty of details to iron out. But whether or not it goes ahead, the NTL-Virgin Mobile flirtation illuminates three big trends in telecoms.

The first is the race, now under way between cable operators and traditional telecoms firms, to provide a "quadruple play" package of fixed-line telephone service, broadband internet, television and mobile telephony. Cable operators in many parts of the world have offered the "triple play" of telephone, broadband and television for some time. This has prompted telecoms firms, wary of losing customers, to start upgrading their networks so that they can deliver TV.

Since telecoms firms typically offer mobile-phone services too, by adding TV they could leapfrog the cable operators and offer a bundle of four services. In response, cable operators such as NTL are moving into mobile. They have the advantage that it is much easier for cable operators to add mobile telephony to their bundles than it is for telecoms operators to move into television—a step that requires expensive new infrastructure and complex deals with content producers.

Hence the second trend: a rash of deals between cable operators and mobile operators—particularly those like Virgin, without ties to fixed-line telecoms firms. In America, Sprint Nextel, a big mobile operator, announced a deal in November with the country's four biggest cable operators, Comcast, Cox, Time Warner and Advance/Newhouse. This will allow the cable firms to add mobile telephony to their existing service bundles later this year, and will also enable Sprint to provide video clips and other content to mobile subscribers. Similarly, in Belgium, Telenet, a cable operator, has struck a deal with BASE, a mobile operator; in Switzerland, Cablecom has teamed up with Sunrise; and Japan's biggest cable firm, Jupiter, has been talking to Vodafone's Japanese arm about buying capacity on its mobile network.

And this highlights the third trend: the evolution of the "mobile virtual network operator" (MVNO) model, pioneered by Virgin Mobile, in which a company sets up as a mobile operator without actually building a network. Instead, it teams up with an existing operator, piggybacks on its network and resells service under its own brand. To start with, notes Carrie Pawsey of Ovum, a consultancy, most MVNOs offered cheap, no-frills voice calls and text messages. As a result, many operators were reluctant to open their networks to MVNOs for fear of cannibalising their own revenues. "But the tables are now turning," says Ms Pawsey. Operators have realised that MVNOs can help them capture customers in segments where their existing brands do not reach. The cable companies' desire to move into mobile, and the emergence of big media companies such as Disney, ESPN and MTV as MVNOs, means that operators are now in the position of competing to attract the most attractive MVNO partners.

In this sense, the NTL-Virgin deal is somewhat unusual, because rather than becoming a "mobile virtual network operator" itself, as other cable operators are doing, NTL simply plans to buy an existing one. That is because doing so will give it access to Virgin's brand, which has far more appeal to consumers than NTL's brand, which has been tarnished by years of low investment and poor customer service, notes Stephen Pentland of Spectrum, a strategy consultancy. The resulting "brand refreshment" will, he says, improve NTL's ability to compete with its big rivals in Britain, BT (the telecoms incumbent, now moving into TV) and BSkyB (a satellite-TV provider that is now moving into broadband and telephony).

All of this, of course, assumes that consumers really do want to buy all four quadruple-play services from a single

firm. In fact, says Mark Page of A.T. Kearney, a consultancy, the benefits of the quadruple play accrue mostly to operators, via reduced overheads and greater customer loyalty (since deals that combine so many services are a hassle to withdraw from). Its appeal to customers, aside from the potential for discounts, is unclear. But the whole industry has decided that quadruple play is the future. Expect more deals.

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Airlines in India

Oasis for Sahara

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The first big takeover in Indian aviation will not be the last

Reuters

Goyal's business is taking off

COMPARED with their elderly and decrepit American cousins, India's private airlines are the very picture of robust youthfulness. But they have their woes too: an acute shortage of pilots, rising fuel and labour costs and, above all, surging competition. The number of domestic air passengers in India is growing by about 25% a year and is expected to climb from around 20m a year now to 50m a year in the next five years. In response, no fewer than five new carriers have entered the market since August 2003. A further two or three will be added this year. No market could absorb that sort of expansion, and this week the inevitable consolidation began.

On January 19th Jet Airways confirmed that it has agreed to buy its smaller rival, Sahara, for a price of “around $500m” in cash. Jet last year overtook Indian Airlines, owned by the government, to become the largest domestic carrier, with about 9m passengers. Sahara accounts for 12-13% of the market, so the acquisition will take Jet's share, which has been falling because of the new competition, to more than 50%. Jet's chairman and main owner, Naresh Goyal, denied reports that he will turn Sahara into a low-cost airline competing with the new budget airlines, such as Air Deccan and SpiceJet.

Binit Somaia, an analyst with the Centre for Asia-Pacific Aviation in Sydney says the deal makes sense since Sahara is a full-service carrier that flies Boeings, as Jet does. Jet's position as the market leader, with world-class standards of service that make most rivals look shoddy, seems secure for a while. Kingfisher was another potential buyer of Sahara. But it is purely a domestic carrier, with a fleet of Airbuses. It also reportedly proposed to raise some of the price through a share issue. Alok Dalal, of India Infoline, a financial-research firm, says the Sahara group, with interests from housing to financial services to television, faces “a cash crunch”.

A big attraction for Jet may be Sahara's overseas routes. Jet already has a few foreign flights, including routes to London, Katmandu and Colombo. Now it has the chance to steal a march on the newer airlines by expanding further internationally. At present, Indian rules prohibit carriers with less than five years domestic experience from operating international routes.

Speculation may now turn to other carriers and potential mergers. In particular, many analysts expect Indian Airlines to reopen talks with Air India, the national flag carrier, which has no domestic routes, and believes it needs them to be viable. But, according to Tim Coombs of Aviation Economics, a consultancy, Air India should steer clear of domestic routes and focus instead on improving its international services.

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American airlines

Courts and cuts

Jan 19th 2006 | CHICAGO
From The Economist print edition

Northwest is the latest airline to use bankruptcy in a labour dispute

Get article background

AP

Runway rebels

A KNOWLEDGE of bankruptcy law is now as important to the bosses of America's airlines as an understanding of aviation. Bosses of United Airlines got in a huddle this week before a final hearing with the court to allow the airline to quit Chapter 11 next month, ending more than three years' protection from its creditors. United's boss, Glenn Tilton, has used the time to remodel the business, slashing about $7 billion of operating costs, by shrinking domestic capacity and improving labour productivity.

Northwest Airlines is the latest to use the bankruptcy process as a management tool, as it tries to rejig contracts with its unions. On January 17th it asked a judge to throw out its collective-bargaining agreements with its pilots and flight attendants.

Like many of its competitors, Northwest has been bleeding money. Between 2001 and the third quarter of last year it racked up pre-tax losses of $3.6 billion. Although the aviation industry is doing better, the big carriers are still losing a fortune. Continental Airlines started the quarterly earnings season this week by posting a net loss of $43m in the fourth quarter, and said that it expects a "significant loss" in this quarter. American Airlines reported a near doubling of its fourth-quarter net loss, partly because of one-off charges. Meanwhile Southwest Airlines, the leading low-cost carrier, once again demonstrated the superiority of its business, with an $86m fourth-quarter net profit, up 54% on a year earlier.

Unlike most of its competitors, Northwest's problems are not caused by brutal competition in its home markets. Its biggest hubs are in its home city of Minneapolis, as well as in Detroit and Memphis. Glenn Engel of Goldman Sachs, a bank, says that these markets are the right size and in the right places: big enough to bring in good revenues, but too small and far away from the coasts to attract much competition from low-cost carriers. But, cushy local markets (and its lucrative clutch of Asian routes) allowed Northwest to let its costs drift out of control.

Once fuel costs rose and overall demand tumbled right after the 2001 terrorist attacks, Northwest had the same need as America's other "legacy" airlines to cut costs and shed capacity. Its unions feel they have already made big concessions by agreeing to temporary pay cuts and a pension freeze. But Northwest says more needs to be done—permanently—if the books are to be balanced. It is hoping the courts will help, as they did with United and US Airways.

Now that many of its rivals have restructured their contracts, says Northwest, its costs are even more out of whack. Dan Kasper, an industry consultant testifying on Northwest's behalf, claimed this week that the airline's unit labour costs are 71% higher than the average for low-cost carriers, and "far and away the highest in the industry". Northwest has said that it hopes to slash its annual costs by $2.5 billion a year, with $1.4 billion of that coming from slimmer contracts with unions. It has made some progress in negotiating new deals with its ground crews. But the most important contracts are those with the two toughest unions, representing pilots and flight attendants. A deal could take a while yet.

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Economist.com BUSINESS

Executive pay

Book of revelations

Jan 19th 2006
From The Economist print edition

New ideas from the regulators for disclosing managers' pay

Get article background

Outsiders' rewards
Boards' independent directors' total compensation*
top ten 2004-05, $m

XL Capital	8.63
WellPoint	7.86
Telewest Global	7.10
Genentech	7.05
ImClone Systems	7.00
Fannie Mae	5.71
MannKind	5.52
UnitedHealth Group	5.45
Target	5.02
Kos Pharmaceuticals	4.97

*Sample of 2,054 of the largest US companies (median $800,000)
Source: The Corporate Library

IT IS 14 years since America's Securities and Exchange Commission (SEC) last changed its rules on corporate disclosure of top executives' pay. In the meantime, other countries (such as Britain) have introduced more demanding standards and Americans have grown increasingly agitated by reports of Godzilla-sized pay packages that often bear little relation to a company's performance. Michael Eisner, the former boss of the Walt Disney Corporation, has become emblematic of this sort of excess. He was a genuinely outstanding manager during the first part of his more than 20 years at the top of the firm. But he was then paid $800m over a 13-year period in which his company's shares did worse than government bonds. Investors claimed they had not realised how richly Mr Eisner was being rewarded.

On January 17th the SEC's five-man board unanimously approved new proposals for increased disclosure of executive compensation. The public now has 60 days to comment on the proposals, after which they could become mandatory as early as the 2007 reporting season. The focus is on providing investors with a single number for the total remuneration of the chief executive, the chief financial officer and the three next-highest-paid executives. The information that is available today is often spread confusingly around several filed reports. In some cases, says Christopher Cox, the SEC's chairman, “disclosure obfuscates rather than illuminates the true picture of compensation.” The SEC says it will require that disclosure “be provided in plain English”, but refrains from saying who will be the arbiter of that.

Obfuscation is rife in three areas in particular—pensions, perks and deferred pay—and the SEC addresses all of them. The new rules will improve the disclosure of top executives' retirement benefits. Currently, it can require an academic study to work out the real figures. Research published last year by Lucian Bebchuk and Robert Jackson of Harvard University put the median value of the pension pots of a sample of top chief executives at $15m. Mr Bebchuk says that companies' “massive use of defined-benefit pension plans [for their top executives] has been partly motivated by a desire to provide chunks of performance-insensitive pay under the radar screen.”

Another way to get rewards under the radar screen is via perks. One of the most popular for American chief executives is the corporate jet. A recent study by David Yermack, a professor at New York University's Stern School of Business, found that the private use of company aircraft is “the most costly, and fastest-growing, fringe benefit enjoyed by major company CEOs.” At present, companies have to disclose perks to individuals in excess of $50,000, valued on the basis of their “aggregate incremental cost” to the company. That can take an executive to far-distant golf courses many times over without showing up on shareholders' radar screens. Mr Yermack found a strong relationship between chief executives' private use of a corporate jet and golf, in particular to membership of the prestigious Augusta golf club in Georgia. On the other hand, he found an inverse relationship between the private use of company's jets and its stockmarket performance. The SEC proposes reducing the threshold for disclosing perks from $50,000 to $10,000.

Severance pay received by departing chief executives and deferred compensation schemes are other dark areas on to which the SEC promises to cast some light. Companies are currently under no obligation at all to reveal deferred compensation, which enables executives to shift their individual tax liabilities to the company.

Combining numbers of this kind into a single headline figure could provide some shocks. “The numbers in total will surprise,” says Pearl Meyer, founder of an eponymous firm of compensation consultants. But they may not cause chief executives' pay to fall. On the contrary, it could rise more rapidly by pushing up the benchmarks against which pay is set.

Controls are in the hands of the non-executive board directors who appoint and decide on the remuneration packages of their top executives. For the first time, the SEC is going to require that companies reveal how much these people in aggregate are being paid. Here, however, the numbers are likely to be surprising for a different reason. A study published earlier this month by the Corporate Library, a governance watchdog, found that the median total compensation of large companies' groups of outside directors was just over $800,000, a figure that the report's author, Paul Hodgson, describes as “moderate”, given that the average number of such directors is eight. Shareholders, however, may not consider it good value for money until these directors show some of the same moderation when setting the pay of their executive colleagues.

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Economist.com **BUSINESS**

Face value

Still livin' on the edge

Jan 19th 2006
From The Economist print edition

REX

Takafumi Horie, dotcom challenger of Japan's corporate elite, may have taken a step too far

IN A land of dark-suited, largely anonymous executives, it is hard to miss the jeans, sneakers and spiky hair of Takafumi Horie, founder of livedoor, an internet and finance company. A survivor of the internet bubble in the late 1990s, the brash 33-year-old is known for his outspoken defiance of old-style corporate Japan—as well as his love of the spotlight and gorgeous women. After starting his first internet company, aptly named Livin' On The Edge, a decade ago when he was still a student at Tokyo University, he dropped out of school to ride the internet wave, advising like-minded students to do the same.

Even in its early days, people took note of his company, tucked away in the back streets of Shibuya, Tokyo's hotspot for the young. Since then, Mr Horie has made a fortune: first by listing his company on Mothers, a stockmarket for start-ups run by the Tokyo Stock Exchange, and then by using the profits to buy livedoor, a defunct internet-service provider. Chiefly through financial engineering (his company, renamed livedoor in 2004, has split its stock 30,000-fold) and a succession of often surprising mergers and acquisitions, the market value of the empire Mr Horie built rose to about ¥930 billion ($8 billion) at its peak. Livedoor controls around 50 companies, including an accounting-software house, an online travel agency, a securities company, a mail-order retailer and a second-hand car firm. In the year to last September livedoor's profits quadrupled, to ¥15 billion.

Yet on January 16th it was Mr Horie who was taken by surprise. His company, now located in Roppongi Hills, a prestigious Tokyo landmark, was raided by prosecutors and investigators from the Securities and Exchange Surveillance Commission (SESC), on suspicion of securities-law violations. They also raided his home in a probe that lasted until dawn.

The investigation is centred around livedoor Marketing, an advertising affiliate, which is suspected of having deceived the public in October 2004 by announcing that it would buy Money Life, a publisher, through a share swap —when it already controlled the firm through a private-investment arm. If the deception is proven, that would amount to market manipulation, a serious offence. Prosecutors also suspect livedoor Marketing of fiddling its accounts so as to boost its share price. Investigators are digging to see the extent of Mr Horie's involvement.

Such was the shock caused by the investigation that on January 17th livedoor shares lost ¥100 billion in stockmarket capitalisation, while the benchmark Nikkei share index saw its largest one-day drop since last April

(see article). The scandal sent politicians scrambling for cover. Mr Horie had stood for election last September as an independent, but one strongly backed by Junichiro Koizumi, the prime minister. Mr Horie was a vocal supporter of Mr Koizumi's plans to privatise the post office—the central issue of the whole campaign. He took on Shizuka Kamei, one of the staunchest opponents of Mr Koizumi within the ruling Liberal Democratic Party, and lost.

While many locals, especially the smirking corporate old-guard, seem already to have judged Mr Horie and condemned him, he still has support. After all, financial jiggery-pokery is a pretty traditional activity in Japan. “Everyone in the international community is watching this closely, because of concerns that this could represent selective enforcement against an aggressive young entrepreneur,” says a foreign lawyer based in Tokyo.

Waking up Japan

If the prosecutors make their allegations stick, it would be a huge setback for a man who has helped shake Japan out of its stolidity. Mr Horie's first real brush with fame came in 2004 during a crisis in baseball. The rising popularity of soccer meant that baseball was losing fans and money. When one of Japan's two baseball leagues was threatened with collapse and the players went on strike, Mr Horie stepped in—offering to buy a cash-strapped team and promoting new ideas to revitalise the sport. His actions prompted other investors to get involved. Although Mr Horie did not ultimately buy a team, he won a reputation as the man who saved Japanese baseball.

Mr Horie also introduced to Japan the hostile takeover, with his brazen bid to take a controlling stake in Nippon Broadcasting System (NBS), a radio station—which, because of a complicated system of cross shareholdings, was regarded as a bid to gain control of Fuji Television, Japan's biggest commercial television station. Fuji fought a bitter and emotional battle over the airwaves and in court against the interloper; while livedoor fought cunningly by skirting the rules—buying shares during after-hours trading, enabling it to avoid disclosure. The Financial Services Agency somewhat belatedly plugged the loophole. The two-month conflict was finally resolved last April, through an amicable settlement in which livedoor sold its stake in Fuji (for a tidy profit), and Fuji made an investment in livedoor. Mr Horie's actions helped change the way Japanese companies do business and have prompted other high-profile hostile bids. Yet there has also been a backlash against the financial liberalisation that Mr Horie has taken advantage of. Under current law, foreign companies can only buy Japanese firms with cash, rather than using their own shares. This rule was due to be scrapped. But after the livedoor-Fuji battle, the government decided to postpone the change for another year.

Mr Horie's emblematic status ensures that he has been at the heart of the unresolved struggle in Japan between those who look to markets to determine such things as who should own companies and those who think that Japan's stockmarket today is overrun by short-term adventurers and the companies that cater to them. The chances of a backlash, especially from the corporate old-guard, will depend on whether Mr Horie continues to live on the edge, or whether he has just walked over it.

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Economist.com BUSINESS

News Corporation

Old mogul, new media

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Reuters

Can Rupert Murdoch adapt News Corporation to the digital age?

IN JUNE 2005 Ross Levinsohn, head of new media at News Corporation, a media conglomerate, presented an internet strategy to a gathering of the company's top managers. It was a daunting prospect: many of them were deeply sceptical about the internet, having watched the dotcom bust of 2000-02. Sure enough, Mr Levinsohn found himself interrupted. “We really can't do that,” objected a senior executive. Before Mr Levinsohn could respond he heard another voice: “What do you mean, we can't do that? Of course we can do that.” It was Rupert Murdoch, the firm's chairman and chief executive.

In his 74th year, Mr Murdoch is very much in charge of the global media group he constructed over the last four decades. But he and his firm face two fundamental issues that relate to News Corporation's traditional media businesses. The first is what to do about the emergence of the internet, both as a medium in its own right, and as a way to distribute media content. The second is how News Corporation's portfolio should be best configured in response to rapidly shifting technologies related broadly to digitisation. Its film and television production units are vulnerable to digital piracy; its broadcast-television business is losing advertising revenue to the internet; and the satellite-television distribution businesses face a stronger cable industry and new entrants. The company's challenge is typified by, but not limited to, its newspaper business—it owns dozens of titles. Last year Mr Murdoch warned in a much-noted speech that the industry would inevitably decline if it fails to adapt to the internet.

Searching for answers to these problems, Mr Murdoch spent $1.4 billion on three young internet companies in 2005, which, together with News Corporation's existing websites, now form Fox Interactive Media, the division that Mr Levinsohn runs. On the internet, News Corporation has now moved ahead of its big traditional media rivals, with the exception of Time Warner, which agreed to be taken over in 2000 by AOL, an internet-access provider. But can News Corporation lead the way for other “old” media and successfully navigate its way forward?

It might seem an unfair question. Compared with its past, News Corporation is calm and profitable. It is convinced that it needs scale and a broad range of businesses embracing both content and distribution—it has no intention of splitting itself up. In the past couple of years it has made heavy investments in satellite television in America and Italy. Those bets seem to be paying off. Most of its businesses are thriving and many are throwing off large quantities of cash. The company's revenues and profits are growing at a double-digit rate, faster than rivals'.

Investors are unimpressed, however. That is partly because they are so gloomy about traditional media companies' prospects: they reckon that the internet is stealing its audiences and that new technologies will combine to wreck established business models (see chart).

Some of the reason has to do with Mr Murdoch himself. Investors are fearful about who will lead the company after him (see article). But the really big issues are how the company will adapt to the internet and the rise of digital media. The problem with creating new business models for the internet and a digital environment is that these can cannibalise existing, more lucrative businesses. One of the biggest problems for News Corporation's film- and television-production business is digital piracy. At the moment Hollywood film studios wait for five months after releasing a film in cinemas before sending it out on DVD, which leaves their content extremely vulnerable to pirates. News Corporation is looking at bridging that gap by offering video-on-demand. But it is difficult to price such an offering to be as profitable as a DVD, and without angering powerful retailers, such as Wal-Mart.

Keeping up with technology in one bit of News Corporation's business sometimes damages another part. To maintain the attractiveness of satellite television, for instance, News Corporation has subsidised digital video recorders for its customers, which allow them to record programmes and watch them when they like. DVRs, as they are known, are disruptive for advertising-funded television, however, because they allow people to fast-forward through advertisements.

“In content, we could not be happier,” says Mr Murdoch. News Corporation's film studio came second for box-office receipts after Warner Brothers in 2005 and it claims the highest margins in Hollywood. Its TV studio is a leading producer of prime-time programmes. Its cable channels are growing fast, and Fox News, especially, continues to benefit from America's divided politics and the war on terror.

“Distribution systems, on the other hand, are proliferating,” says Mr Murdoch, and “while that is great for content, it raises questions about the long-term economics of distribution.” The internet is emerging as a distribution system in its own right, and telecoms firms are already trying to deliver television using internet technology. News Corporation has spent enormous amounts of money and energy over the years on satellite-television platforms in America, Britain, Italy and Latin America. Now investors are worried that satellite is losing its competitive advantage.

Its most immediate challenge is from the cable industry, which has invested heavily in its infrastructure and is now offering a bundle of digital television, broadband and voice service. At the moment, satellite cannot offer this “triple-play” option: it has only TV. Neither can it sell as full a video-on-demand service, because it beams the same television signal across whole regions. That will become a serious drawback as video-on-demand quickly becomes a standard product, says Craig Moffett, an analyst at Sanford C. Bernstein in New York. In Britain and Italy satellite also has to vie with attractive free digital-terrestrial television services.

In response, News Corporation is rushing to add broadband and voice to its satellite-television products around the world. In Britain BSkyB bought Easynet, a broadband internet-access company, for $385m in 2005. News Corporation is also working on a way to add broadband to DirecTV's portfolio, and expects to announce a solution in the near future.

As for video-on-demand, News Corporation plans to store as many popular television shows and movies as it can on digital video recorders for instant playback. For more obscure material it will provide a broadband option. In Britain it took a first step in this direction on January 10th by allowing its subscribers to download films and sports highlights from the internet on their home PC free of charge.

The most challenged of all of News Corporation's divisions is its newspaper business, which contributes one-fifth of its operating income. Newspapers are suffering from the internet more than the rest of “old” media, as classified advertising moves online and young people are using the net to get their news. No other media conglomerate owns newspapers in any significant number. Mr Murdoch recently sold the educational supplements of the British *Times* because he thought they were too dependent on classified advertising. But he does not appear to have any bolder solution. “Despite his speech, only a tiny fraction of News Corporation's energy appears to be going into securing its newspapers' future online,” says Simon Waldman, director of digital publishing at the *Guardian*. In Britain the Murdoch-owned *Sun*, *Times* and *News of the World* together attracted 6.7m unique visitors in November 2005, only the same as the *Guardian* alone, and far fewer than the 21.4m who visited the news site of the BBC, a publicly

funded broadcaster.

Many investors would like Mr Murdoch to reduce News Corporation's exposure to newspapers. The main reason that he does not, says a shareholder, is that he's "an empire builder who refuses to sell things". This investor would also like the company to sell its television stations, which are struggling to grow because America's advertising market is mature and because advertisers are moving money away from TV to the internet. One executive at the company agrees that "we've never been very good at selling things, except under duress."

Mr Murdoch says that he will not get rid of newspapers. "That may be emotional", he says, "but we're a communications company, not just a content company, and we want to improve the world." Owning newspapers, of course, has given the group clout with politicians and regulators. He argues that a sale would lose a large slice of value on capital-gains tax.

If he is a stickler on that front, there is no denying that Mr Murdoch appears to have become an internet evangelist for his group as a whole. The first time he invested enthusiastically on the internet, everything ended disastrously. During the boom of the 1990s, he refused to join the frenzy until 1999, then spent hundreds of millions of dollars on ePartners, a dotcom investment division, only to wind it down a year or so later.

This time around, his interest in the internet started last year after he noted that America's economic growth was not showing up in advertising on TV, radio or print, but that the internet was starting to grab a meaningful share. At the same time, he saw that broadband internet access was becoming widespread. Once most people have broadband, he reckons, they will want video as well as music, still pictures and text. News Corporation owns a huge amount of the entertainment and sports programming that young people are likely to want to access via broadband.

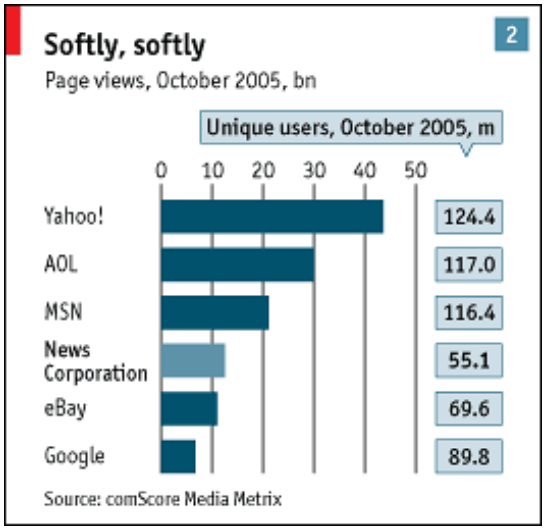
A flurry of deals followed that insight. None of them is transformative—the amounts involved remain small by comparison with News Corporation's huge turnover or its $54 billion market value. But the message is clear: News Corporation "gets" the internet and is determined to embrace it.

This came across loudest in July 2005 when News Corporation surprised everyone by buying Intermix Media, owner of MySpace.com, a social-networking site, for $580m. The following month it acquired Scout.com, a college sports site. And in September it bought IGN Entertainment, a video-gaming and entertainment site, for $650m. More such acquisitions are likely to follow. Richard Bilotti, media analyst at Morgan Stanley, says the firm may spend $500m to $1 billion a year in the next three to five years.

Do you have a MySpace?

The sites' combined traffic, added to News Corporation's own web properties, FoxSports.com, FoxNews.com and Fox.com, has pushed News Corporation up among the giants of the internet (see chart 2). Google, an internet search firm, is taking note of News Corporation's purchases. Mr Murdoch has passed on to colleagues that Eric Schmidt, chairman of Google, told him that buying MySpace.com will prove to be the best deal of his life. That News Corporation has chosen to buy an unusual site where users create the content shows that the company is not merely reproducing itself online, but thinking differently about the future of the internet.

Since May 2005 the number of people who visit MySpace.com each month has grown from 16m to 27m, and 150,000 people are registering each day. Like Google before it, MySpace.com has entered the English language. Its appeal is that its members create an anarchic mix of their own content. The site is a collection of individuals' homepages with photographs, music, links to friends and blogs.



As an internet business, MySpace.com considers itself to be an entirely new breed. Chris DeWolfe, its co-founder, says he wanted the company to take inspiration from sociology as well as from technology, and for that reason he based it in Los Angeles rather than Silicon Valley. The community has grown virally, with no advertising. Some of the photographs verge on the pornographic, and MySpace.com has about ten people in a room at its headquarters in Santa Monica, Los Angeles, weeding out explicit photographs. With its young members, its 24-hour discussion groups on everything from graffiti to independent film-making, and its thousands of undiscovered bands, MySpace.com has the ambition not just to be useful, like Google, MSN or Yahoo!, but cool.

While no one doubts that News Corporation has tapped into a powerful social phenomenon, some people question if there is much money to be made from it. The company expects to make $300m of revenue on the internet this year, and Mr Murdoch said he wants the company to make $1 billion from it in five years' time. “MySpace has been run by creative types who have not thought much about earnings and are frightened of being corporatised,” says Mr Murdoch, “but now their job is not just to grow but to monetise traffic.” MySpace.com is profitable, but it has not translated its popularity into big advertising revenues. IGN, on the other hand, the most popular site on the internet for young men, has a more developed business model based on advertising. Together the sites make modest tens of millions of dollars in profits.

Now News Corporation will try to convert their traffic into more advertising revenue. If it does so too obtrusively, there is a risk that their free-spirited members will move somewhere else. To avoid that happening, Mr Levinsohn plans to create scarcity of space and to charge a high price. The premium will be justified, he says, by the attractively young demographic—predominantly 13 to 34—of the audiences, and the amount of information News Corporation has about each user, which will allow advertisers to target precisely. Despite its huge audience, MySpace.com still has a lot to prove to advertisers, says Rob Norman, director of interaction at Group M, the media-buying arm of WPP. “It's not yet clear what the value of user-generated content is to brand owners,” he says.

Owning internet properties is also a way for News Corporation to establish its content online. Before the company started talking to MySpace.com, the biggest four discussion groups on the site were about three programmes made by Fox, its subsidiary—“Family Guy”, “The OC” and “The Simpsons”—and a film from Fox Searchlight Pictures, “Napoleon Dynamite”. IGN has developed technology to allow the downloading of large video files from the internet. In 2006, as a start, News Corporation will use this to distribute “Family Guy” episodes made exclusively for the internet across Fox's websites. The company is already feeling a marketing benefit from its web communities. One of Twentieth Century Fox's films, “Transporter 2” did far better than expected after being promoted on MySpace.com and IGN.

Nevertheless, it is News Corporation's big legacy businesses that will mostly determine whether the company can adapt to a new era for the media industry. That is why Mr Murdoch will need to keep focusing on making money from television, films and newspapers as well as his trendy new web communities.

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The Murdoch succession

Family affair

Jan 19th 2006
From The Economist print edition

Investors are fretting about who will succeed Mr Murdoch

ON TOP of its strategic challenges, News Corporation faces the tricky question of who will take over from Mr Murdoch. One view is that his eventual departure will be followed by a break-up of the company, because it consists of his particular choice of assets and may prove too unwieldy for anyone else to hold together.

So far, Mr Murdoch's plan to pass control of News Corporation to one of his children is going badly. Last year his eldest son, Lachlan, left the business after losing a power struggle with other (non-Murdoch) senior executives, and his daughter Elisabeth abruptly left BSkyB in 2000. Now only James, at 33 the youngest of his adult children, remains in the business—he is currently chief executive of BSkyB.

Does James want the burden of running the whole company? Executives at News Corporation reckon that he has the necessary ambition, and he has won the respect of shareholders. But with no experience of running any of News Corporation's big American divisions, it is hard to imagine James taking over soon. Investors expect that if anything happened to Mr Murdoch, or if he stepped down, Peter Chernin, the group's chief operating officer, would take over.

Meanwhile, Mr Murdoch has failed to see off John Malone, boss of Liberty Media, whose 18% voting stake is not far off the 29.5% that the Murdochs collectively own. In 2004, to the dismay of shareholders, News Corporation's board agreed to a poison-pill defence to prevent Mr Malone buying more voting shares. Eventually, Mr Murdoch hopes to overcome the impasse by buying back Mr Malone's shares in return for one or more of the group's assets. “We're waiting on him to come up with a scheme that will satisfy his tax issues,” Mr Murdoch says. He rejects the possibility that Mr Malone intends to grab control of News Corporation. “He's a great financial engineer, but he doesn't have the management,” Mr Murdoch says.

For the moment, News Corporation intends to keep its poison pill, even though investors dislike it. News Corporation argues that senior people at big fund-management firms do not have a big problem with the poison pill, and that it is only corporate-governance specialists who are making a fuss. Perhaps, but the company would doubtless like more fund managers to buy its shares. Many will not do so until the poison pill is gone and there is clarity about who will end up in charge.

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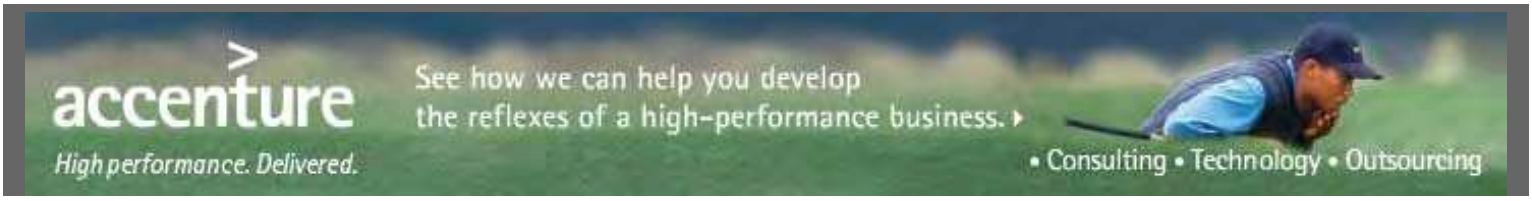
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Emerging economies

Climbing back

Jan 19th 2006
From The Economist print edition

The economies of what used to be called the "third world" are regaining their ancient pre-eminence

SINCE their industrial revolutions in the 19th century, the rich countries of the "first world" have dominated the global economy. By one measure at least, that era may be over. According to estimates by *The Economist*, in 2005 the combined output of emerging (or developing) economies rose above half of the global total.

This figure has been calculated from the International Monetary Fund's *World Economic Outlook* database. We have adjusted the IMF's numbers in two ways. First, we have taken account of China's recent upward revision of its GDP by 17%. Second, we include the newly industrialised Asian economies (South Korea, Taiwan, Hong Kong and Singapore). These countries might well now be classed as developed, but should surely be counted in any estimate of the long-term success of developing countries. If you exclude countries once they prosper, developing economies' share will never increase.

We have used the IMF's method of converting national GDPs into dollars using purchasing-power parities (PPPs) instead of market exchange rates. The latter can distort the relative size of economies, not only because currencies fluctuate, but also because prices are lower in poorer economies (so a dollar of spending in China, say, is worth a lot more than it is in America).

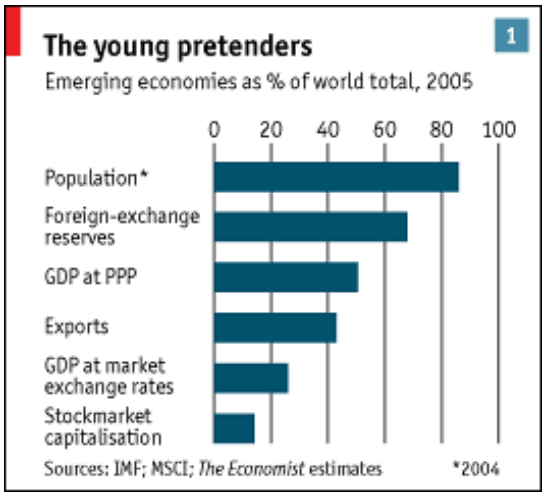
The prices of traded goods tend to be similar to those in developed economies, but the prices of non-tradable products, such as housing and haircuts, are generally much lower. As a result, converting a poor country's GDP into dollars at market exchange rates could understate the size of its economy and its living standards. This is why the IMF uses PPPs, which take account of international differences in prices of the same goods and services, to provide a more accurate measure of the purchasing power of each country's inhabitants.

It makes a big difference. Measured at market exchange rates, developing economies' share of global output has fallen over the past quarter-century, to just 26% last year. Measured at PPP, it has (more realistically) risen, to just over half. Perhaps the best evidence of the flaw in current-dollar figures is that they suggest developing Asia's share of world output was barely higher in 2000 than in 1980, even though it had been by far the world's fastest growing region. The effect of growth was distorted by currency movements.

Admittedly, calculating PPPs is tricky. They are based on surveys of prices around the world. But as Keynes used to say, “It is better to be roughly right than precisely wrong.” Using PPPs provides a more realistic estimate of the balance of output between rich and poor countries. But they are not always appropriate. Trade and financial flows, which, unlike the bulk of GDP, are transacted at market exchange rates, should be converted at those rates into dollars. For businesses too, market exchange rates are relevant for converting foreign revenues and profits into dollars.

But even when measured by market exchange rates emerging economies are flexing their muscles. Last year, their combined GDP grew in current dollar terms by $1.6 trillion, more than the $1.4 trillion increase of developed economies. And there is more to this than just China and India: these two countries together accounted for only one-fifth of the total increase in emerging economies'GDP last year.

Of course, with half the world's output but five-sixths of its population, emerging economies still have incomes per head far lower than the rich world. But by a wide range of gauges they are looming larger (see chart 1). Their share of exports has jumped to 42%, from 20% in 1970. Over the past five years, they have accounted for more than half of the growth in world exports. Emerging economies are now sitting on two-thirds of the world's foreign-exchange reserves and they consume 47% of the world's oil. On the other hand, their stockmarkets still account for only 14% of global capitalisation.



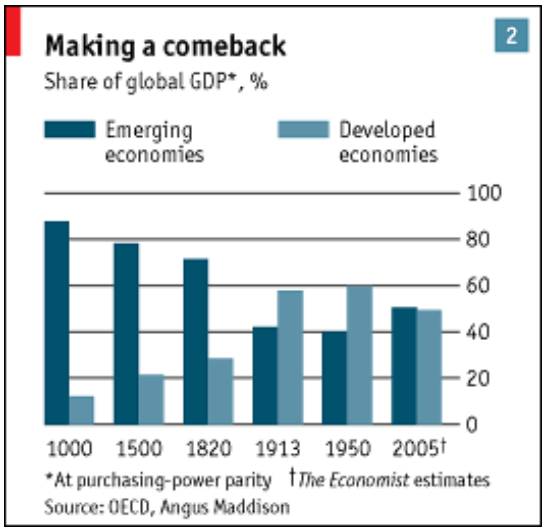
Emerging economies have also become increasingly important markets for companies from the rich world. Developed economies' trade with developing countries is growing twice as fast as their trade with one another. Over half of the total exports of America, the euro area and Japan now go to emerging economies. The EU exports twice as much to them as it does to America and Japan combined.

As you were

The growing clout of emerging economies is in fact returning them to the position they held for most of history. Before the steam engine and the power loom gave Britain its industrial lead, today's emerging economies dominated world output. Estimates by Angus Maddison, an economic historian, suggest that in the 18 centuries until 1820 they produced, on average, around 80% of the total. But they were then left behind by Europe's technological revolution. By the early 20th century their share had fallen to 40% (see chart 2).

The term “emerging market” was coined 25 years ago by the International Finance Corporation, the private-sector arm of the World Bank. For much of the time since, “submerging” has been more apt: look at the succession of crises, from Latin America to East Asia and Russia, in the past decade or so.

Now emerging economies are on the rebound, enjoying their best performance for decades. All 32 economies tracked each week by *The Economist* (see articles) grew in 2005, for the second year running. In every previous year since the 1970s, at least one emerging economy suffered a recession, if not a severe financial crisis. In the past three years, their growth has averaged more than 6%, compared with 2.4% in rich economies. The IMF forecasts that in the next five years they will roll along at just under 6%, twice as fast as developed economies. Extrapolation is risky, but if this relative pace were sustained, in 20 years' time emerging economies would account for two-thirds of global output. Is this likely?



It stands a good chance. Most emerging economies are today in much stronger health, leaving them better able to withstand adverse global shocks. Their economic policies have matured: most have cut inflation, thanks to stricter monetary and fiscal policies; they have generally shifted towards more flexible exchange rates; and many are now running current-account surpluses and have built up weighty foreign-exchange reserves. Structural reforms to open up markets and to strengthen financial systems are also helping to improve the efficiency of investment.

This week the Institute of International Finance, a bankers' association, said that net private capital flows to

emerging markets hit a record $358 billion in 2005. But most countries no longer need this money to finance current-account deficits. Unlike many previous booms, their current expansion has been financed largely by domestic saving rather than debt: their average ratio of foreign debt to exports has fallen from 174% in 1998 to 82% last year.

Beware of hiccups

However, some of the recent boom in emerging economies is due to three factors that may be unsustainable. First, rising commodity prices have given a fillip to producing countries, such as Russia, Brazil and South Africa. Second, low interest rates have reduced debt-service costs—especially important for Latin America, where the debt-to-export ratio is twice as high as the average for emerging economies. And last, exports have been boosted by America's strong import demand. This favourable environment cannot last: interest rates are rising, and American consumers cannot keep spending more than they earn. Emerging economies' energy-intensive heavy industries are also vulnerable to high oil prices. A saving grace is that these risks partly offset each other. A slump in American demand would reduce both interest rates and oil prices.

Perhaps the biggest risk is that the boom may encourage complacency and reform fatigue. Yet further action is needed, from greater fiscal discipline to more flexible exchange rates.

The future expansion of emerging economies will not follow a straight line. It is unavoidable that emerging economies are more prone to economic ups and downs and financial bubbles, as America was during its entry on to the global stage in the late 19th century. However, the long-run prospects for emerging economies as a whole look excellent, so long as their move towards free and open markets and sound fiscal and monetary policies continues. Get these basics right, and developing countries ought to outpace advanced economies. Because they start with much less capital per worker than developed economies, there is huge scope for boosting productivity by importing western machines and know-how.

Confirmation that emerging economies are grabbing a bigger slice of global output will frighten many people in the rich world. It shouldn't: living standards depend on absolute not relative growth. Emerging economies' spurt is boosting global output, not substituting for growth elsewhere. Their vim is fuelling growth in the rich world just when greying populations might otherwise cause it to slow—not only by importing from developed countries, but also by supplying cheaper consumer goods, by allowing multinational firms to exploit bigger economies of scale, and by encouraging a better allocation of resources through increased competition. It is surely better for today's rich countries to have a smaller share of a fast-growing global economy than a bigger one of a stagnant world.

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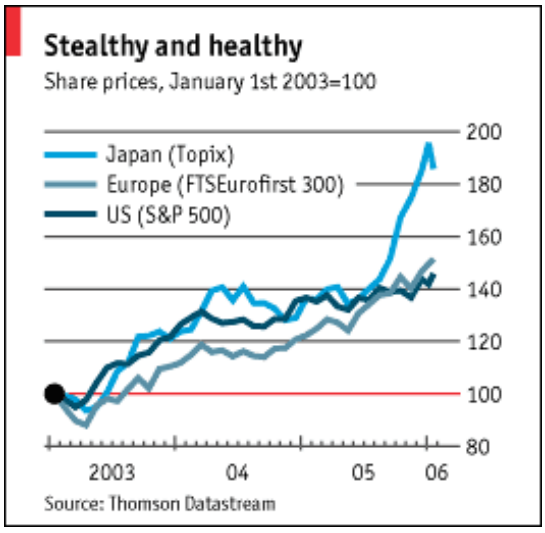
Stockmarkets

Too good to be true

Jan 19th 2006
From The Economist print edition

After an exuberant start to the year, stockmarkets have had a shock



UNTIL this week, a hint of complacency had crept into global stockmarkets. After a three-year rally, it was as if Goldilocks was back for second helpings. In investors' eyes, global economic growth would continue, not too hot and not too cold, with decent corporate profits producing a fourth good year in a row for equities. Such sentiment drove markets up sharply in early January: for those who note milestones, the Dow Jones Industrial Average briefly passed 11,000, within 6% of its peak of 11,723, set six years ago at the height of the dotcom boom. Robert Parkes, a strategist at HSBC, summed up the mood: “Perhaps our biggest concern at the moment is that everything looks too good to be true.”

That was before this week's combination of rising oil prices, disappointments in early fourth-quarter earnings numbers in America and a financial scandal in Japan (see article and article). In the three days to January 18th, the MSCI World index of rich-country stockmarkets lost 1.7%. In Britain, sentiment was also tested by warnings from Mervyn King, governor of the Bank of England, and his deputy, Sir Andrew Large, about the risks of high global asset prices, stoked by low long-term interest rates. They held faint echoes of comments made ten years ago by another central banker about “irrational exuberance” among stockmarket investors.

Such pointers to frothiness in global markets are worth taking seriously. With cheap money sloshing around the financial system, startlingly high levels have been attained in markets of all sorts, including gold—at a 25-year peak—bonds and property. Arguably, the one accompanied by least fanfare has been equities. Yet Japan's Topix index has almost doubled in the past three years, European equities are up by more than 50% and America's S&P 500, despite a sluggish 2005, has risen by 46% (see chart). Emerging markets have done even better.

One of the remarkable aspects of stockmarkets' climb has been its stealth: it has happened even though equities have fallen out of favour among pension-fund managers and retail investors alike. HSBC estimates that investing institutions sold $1 trillion of global equities last year, largely to buy longer-term bonds that more closely match liabilities, such as pension promises. That is quite a headwind. Meanwhile, in many countries individual investors have turned their attention since the dotcom boom from stocks to property. Yet stockmarkets, in the main, have steamed ahead, taking investors' apathy, rising interest rates and higher commodity prices in their stride. How have they developed such stubborn resilience, and how long can it last?

Underlying stockmarkets' good run has been a healthy improvement in corporate profits. After cutting flab in the depths of the bear market, companies quickly returned to sales and profit growth, and handed lots of cash back to shareholders. Only now are investors encouraging them to splash out on capital expenditure and acquisitions, where there is more chance of money being wasted.

Since 2003, global profit growth has been extraordinary. For nine consecutive quarters, operating earnings among constituents of the S&P 500 have grown at a double-digit rate, year on year. That is the longest period of such growth since the last great profit recovery, from late 1992 to late 1995, according to Thomson Financial, a research company. Thomson says that earnings growth in both Europe and America has outpaced share prices. That has cut the forward 12-month price/earnings ratio for the S&P 500 from 26.4 at the peak of the bull market to below 15. European ratios have also fallen.

The profits boom has been fuelled by globalisation. The emergence of China and India, with their vast, cheap labour forces, has weighed on labour costs in the West, as well as keeping a lid on inflation and interest rates. But there is a flipside. The demand for raw materials from China and other fast-growing emerging economies is now posing a threat to profitability, as commodity prices rise. This week, oil prices rose close to $67, their highest in almost four months. That provided a sharp reminder of the sort of cost pressures which, for example, bedevilled fourth-quarter earnings at Alcoa, an American aluminium producer.

There are further reasons to doubt optimistic projections for profits this year. In America, there are signs that pressures on labour costs are mounting. Poor fourth-quarter reports this week from such well-known names as Yahoo! and Intel added to the concerns. And if the dollar falls against other currencies, as many expect, Europe's exporters may be squeezed. European profits growth is already expected to slow to single digits this year.

That said, slower earnings growth would not necessarily trigger a sharp sell-off of shares. According to Thomson Financial, in the year after the end of America's 1992-95 profits boom, the S&P 500 still rose by 20%. With bond yields so low, equities still seem good value to some. Peter Oppenheimer, a strategist at Goldman Sachs, notes that the equity risk premium—investors' reward for being far down the repayment queue if a company runs into trouble—is unusually high.

But it is unwise to be complacent. Risks to the global economy lurk in the shape of a housing-related slump in American consumer demand or a sharp slide in the dollar precipitated by global economic imbalances. Above all, as Mr King has noted, a turn in the credit cycle could have nasty effects on asset markets of all sorts. This is no time for exuberance, rational or not. This week's pause for reflection on the robustness of global stockmarkets came at just the right time.

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Japan's stockmarket

Situation normal

Jan 19th 2006 | TOKYO
From The Economist print edition

Not the first, and probably not the last, cock-up at the Tokyo Stock Exchange

Reuters

Bad day for the Nikkei

AN EMERGING market, it is said, is one from which it is difficult to emerge in an emergency. By that definition, Japan qualifies as the world's biggest. On January 18th the Tokyo Stock Exchange (TSE) shut down trading early for the first time ever, so overwhelmed was it with share orders. News that a brash internet company, livedoor, was under investigation for market manipulation and accounting irregularities (see article) had sparked two days of widespread selling during which the benchmark Nikkei index and the broader Topix both fell by 5.7%.

The exchange's emergency closure 20 minutes early (with curtailed trading announced for the following day, too) leaves what remained of its reputation in tatters, and everyone in government from the prime minister down seething. In November a systems failure caused trading to be suspended for much of the day. Last month, when a broker at Mizuho Securities mis-keyed a share order, the TSE was unable to help reverse it, causing ¥40 billion ($330m) of losses for Mizuho. To atone for these messes, the exchange's president, Takuo Tsurushima, resigned, with two other executives.

Despite capacity upgrades, the exchange has been caught napping by the increase in trading volume that has accompanied a bull market. Much of the increase is accounted for by online accounts, which almost doubled in 2005, to 2.2m. These accounts, used by individual investors, tend to represent great quantities of small orders which take as much processing as big ones.

Livedoor is not even listed on the TSE's main market. But many online traders used its shares as collateral for other margin trades. So when broking firms demanded more collateral, the selling in livedoor spread to other stocks, especially technology high-flyers.

The TSE did not help itself on January 18th by announcing in the middle of the day that it might have to close—that merely encouraged a greater surge of orders. All the same, the next day things looked better. Volumes were down a bit, and shares even recouped about half the losses. The priority now is to prevent many more disasters. The foreign brokers that profited from Mizuho Securities' fat fingers say they will give the money back if it goes to revamping the TSE's trading systems—an urgent enough task, you would think, not to have to depend on these gentle firms' charity. The question is whether the exchange's executives—and Fujitsu, the company in charge of the systems—are up to it.

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Securities litigation

Dead money

Jan 19th 2006 | NEW YORK
From The Economist print edition

Some things even people on Wall Street will not do for a buck

MAKING money from shares has never been easy—not even, as American investors have found, when the authorities hand it to you. At the end of 2002, Eliot Spitzer, New York's attorney-general, trumpeted a settlement with Wall Street firms over their equity analysts' conflicts of interest. Next week Francis McGovern, a Duke University law professor, is expecting to file a report in a New York federal court on the fate of the $440m (one-third of the total) reserved for aggrieved investors. Fewer than half of the 76,000 eligible for reimbursement have filed a claim. Only about 20,000 will receive a cheque. So low are the standards for such programmes that this is being hailed a success.

The claims procedure was less onerous than most. The investment banks agreed on their contributions and on which companies' shareholders would be compensated, and provided a list of buyers to the court. Those eligible should have all received notice, seen advertisements or consulted a website. Mr McGovern even published yet another notice. Assuming that investors had stuck with the same broker, applying for reimbursement required merely the signing of a one-page form.

Yet many did not. Maybe some people did not feel comfortable signing a legal document without professional advice. Mr McGovern suspects that many thought the potential payoff too trivial to pursue—although that seems less likely in the analyst settlement than in others. Perhaps some investors never received notice of the chance to claim. Shares are often held in the names of broking firms or banks, which have no fiduciary obligation to pass on notices of settlement. Those that do, often find themselves swamped by confused clients and are asked, in effect, to provide legal advice that they ought not to give.

The process was trickier for those who used different brokers to buy and sell. Paperwork would have to be provided to substantiate their losses—not easy years after the event. Lots of potential claimants were excluded, notably those with no record of using tainted research (although analysts' puffery inflated the price for everyone). Among this group were investors in index funds—such as those of Vanguard, a mutual-fund company with a reputation for counting the pennies, which would surely have claimed if it could.

Other big institutions habitually pass up opportunities to retrieve from the courts what they have lost in the markets. A study by James Cox, a colleague of Mr McGovern's at Duke, of 118 securities class-action suits between 1995 and 2002, published in the *Stanford Law Review* last month, concludes that 72% of institutions never claim their full share of the proceeds. Mr Cox offers several explanations: institutions' distaste for a form of litigation that, as they see it, benefits mainly lawyers; low expected gains; and the cost and hassle of claiming. Institutions using several brokers would find it a nightmare to reconstitute trading records to show that purchases and sale of shares tally with the publication of flawed research.

Merely keeping up with all the settlements is a job in itself. Garden City, a legal-administration service, recently sent out a blanket proposed settlement for 298 initial public offerings that took place in 1999 and 2000. WorldCom alone is due to pay holders of 48 different securities: claims, backed by trading records, must be filed both with the Securities and Exchange Commission and with the private law firms handling litigation in New York.

There is no complete public list of pending litigation. Institutional Shareholder Services, of Washington, DC, which tracks and responds to lawsuits for institutions, says its business has grown faster than its wildest projections. For individuals, there is no help and the process can be maddening. In 2003, for example, Lucent, a telecoms-equipment maker, agreed to a $517m settlement. Of this, $100m plus expenses went to plaintiffs' lawyers. The rest was split among shareholders who could satisfy numerous conditions and use various formulas to calculate an applicable loss, which by the time the cheques arrived last year worked out at as little as a cent on the dollar.

A unique case? Petitions for repayment from a $67m fund are due at the end of March for shareholders of St Paul Travelers, an insurer. These include the masses who owned shares in Citigroup in 2002, when it spun off Travelers. Calculating a potential loss means wading through phrases like “an authorised claimant's recognised loss per share shall mean 45% of the lesser of...” You get the idea.

The low rate of claims could prompt a number of responses. From a market perspective, the cost and complexity looks simply too high. From a legal point of view, Mr Cox says, a case could be made that pension funds and other institutional investors are violating their fiduciary responsibilities when they do not try to get their money. Tellingly, the organisations that provided the data for Mr Cox's study have now cut off the supply. Maybe they fear class-action suits to come.

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German property funds

Black Tuesday's aftermath

Jan 19th 2006 | FRANKFURT
From The Economist print edition

The peculiar flaws of German open-ended property funds

WHAT crisis? That is how some peddlers of Germany's open-ended property funds have responded to reactions, verging on panic, to the closure of two such funds since early December. Admittedly, the closures are only temporary, pending the revaluation or sale of assets. But to investors who had regarded such funds as rock-solid, entrusting them with €88 billion ($104 billion), they were a nasty shock. Now the government is threatening to rewrite the rules under which the funds are sold. The Investment Management Association (BVI) will try to pre-empt that next week by unveiling its own list of self-regulatory measures.

The problems started in 2003, when parent banks began to bail out funds that were set to lose investors' money: Dresdner Bank, HVB and Deka Bank each took ailing property on to their own books to pump fresh liquidity into the funds and prevent huge withdrawals. Attempts have since been made to match the prices of the funds more closely to the market value of the properties. But they have failed to address the products' fundamental weakness: that a lumpy property portfolio is being sold as a cash asset, tradable at daily prices with limited downside risk. Something had to snap.

It did so on December 13th, predictably dubbed “Black Tuesday”, when DB Real Estate, a subsidiary of Deutsche Bank, closed grundbesitz-invest, a €6.2 billion property fund, for a revaluation expected to last two months. It had caused a run on the fund five days earlier by signalling the revaluation. The closure was the first in the 40-year history of open-ended property funds and prompted an outcry. Deutsche Bank tried to limit the damage by promising to compensate some investors. For many, that just added fuel to the flames—as well as irritating the bank's shareholders, because it had no legal obligation to help investors, even though doing so had since 2003 become the norm.

Until this week it seemed that the industry would weather the storm and go back to its old, untransparent ways. But then Scope, a specialist rating agency, downgraded another fund, KanAm US-grundinvest, because of an investigation in America into the Mills Corporation, an associated company. A subsequent flurry of withdrawals prompted the fund to close for three months to restore liquidity. BaFin, the German financial regulator, found the downgrade and its timing unjustified, but Alexandra Merz, a managing director at Scope, insisted she was doing her job.

Now there are fears of more withdrawals and more closures. There is little doubt that the property-fund business needs reform, but how? The BVI is likely to suggest better and more independent monitoring, and having non-bankers on funds' supervisory boards. Another suggestion doing the rounds is to limit funds' tradability—to a few days a month, or with penalties for big withdrawals—which would make them less vulnerable to runs. It would also threaten their mass appeal. That may be no bad thing.

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Banking in Poland

Tussles with Brussels

Jan 19th 2006 | WARSAW
From The Economist print edition

Polish protectionists take on the European Commission

BIG business and bossy outsiders are rarely popular, especially with economic nationalists, of whom Poland's new minority government has plenty. They are holding up the €15 billion ($18 billion) takeover of Germany's HVB by Italy's UniCredit. This is just the sort of cross-border deal that Europe's fragmented financial industry needs. But in Poland it involves the merger of the second-biggest bank, Pekao (owned by UniCredit), with the third-biggest, BPH (controlled by HVB).

The EU's competition commissioner, Neelie Kroes, cleared the deal in October. Ms Kroes looked at its effects in Poland, but concluded that the country's banking market would still be competitive enough. But the Polish government is blocking the deal nonetheless. Partly, this is because it thinks there will be less competition. It also balks at the loss of around 9% of jobs in the merged banks. And it is indignant that the country's biggest bank will be run from a regional headquarters in Austria.

But the real reason is that the takeover is bad news for state-owned PKOBP, until now Poland's biggest bank. The new government wants to force UniCredit to sell some of its Polish assets, making the new bank smaller and less threatening. Naturally, it dislikes foreign bureaucrats telling it that all this is quite illegal.

Many Polish officials and politicians seem unaware that EU membership has limited their control over their own country. Told that the EU claims “exclusive competence” in competition policy, a spokesperson for the treasury ministry replies crisply: “Maybe they do.” The chairman of the parliament's finance committee, Wojciech Jasinski, of the ruling Law and Justice party, said this week: “What the commission thinks should not have any impact on the approach of our government.”

The politics may be compelling, but the legal case against the deal looks flimsy. The only grounds for blocking it are prudential—if it involved dirty money, or threatened the stability of the financial system. Officials at the National Bank of Poland, which supervises banks, agree that there is no sign of this. But the central bank is under political fire from the new government, which dislikes its tight-money policy. One government appointee on the bank's council, Cezary Mech, has already said he will vote against clearing the takeover, apparently on purely political grounds.

If Poles are spoiling for a fight with Brussels, the feeling is mutual. Ms Kroes's office sent a peremptory letter to Poland this week, asking for an explanation by January 23rd of official footdragging. Under EU law, the commission can issue a ruling that a Polish court would have to uphold, allowing the deal through. In theory, anyway. In practice, however, it could take three uncertain years. “That's the trouble with the EU admitting countries without a mature court system,” says a Warsaw lawyer close to the case. “Polish judges...don't understand cases like this.”

Delay and controversy would be bad for UniCredit, which is eager to get going in central Europe's biggest and most promising banking market. PMR, a Cracow consultancy, says Polish banking portfolios are bursting at the seams, chiefly thanks to booming mortgage business. So rather than be squeezed between the warring EU, government and central bank, UniCredit is looking for a compromise. A showdown might be an exemplary lesson for someone. But who wants to be the recipient?

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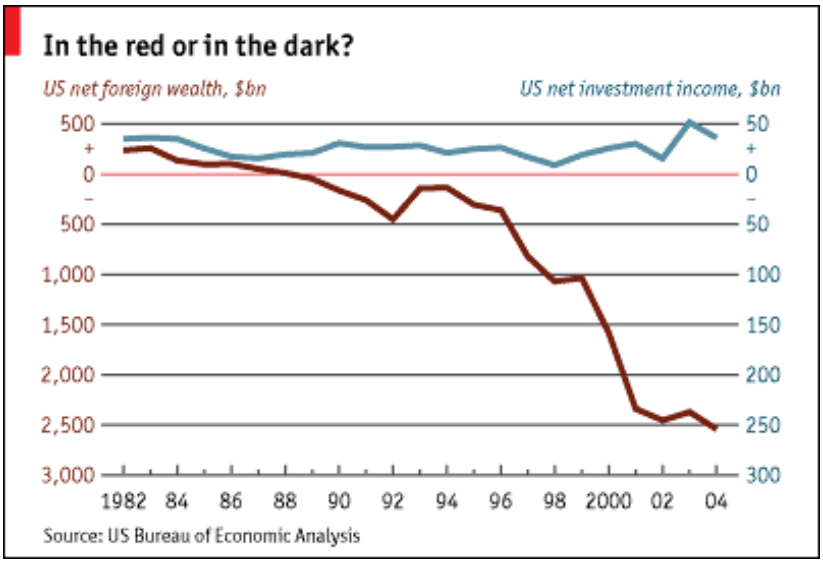
Economics focus

America's dark materials

Jan 19th 2006
From The Economist print edition

The United States' current-account deficit is a figment of bad accounting. If only



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STARE at something long and hard enough, and it will begin to swim before your eyes. Economists have been scrutinising America's current-account deficit for years now, and they are no closer to agreeing on what they are looking at. Now two economists at Harvard doubt whether the deficit even exists. Ricardo Hausmann and Frederico Sturzenegger first put this claim in a working paper* released last November. Your correspondent has blinked twice since then, but the claim has not gone away. On the contrary, it is gathering moss†.

At the heart of the argument is a well-known paradox. In the mainstream view, America is now the world's biggest debtor. Thanks to its chronic trade deficits, it stood $2.5 trillion in the red at the end of 2004. And yet it still somehow manages to earn more on its foreign assets than it pays out to service its much bigger stock of debts: $36.2 billion more in 2004.

Most economists conclude that America earns a higher return on its overseas assets (eg, EuroDisney) than foreigners earn on investments in America (eg, Rockefeller Centre). They don their anoraks, immerse themselves in the data and try to work out why this might be so. Messrs Hausmann and Sturzenegger turn the question on its head. It is not the $36.2 billion of income that is the mystery, they say. The anomaly lies in the $2.5 trillion of debt. If America is still coming out ahead of foreigners, then, contrary to popular belief, it must still be a net creditor. America must have more foreign wealth than we can see.

The two authors have borrowed a name for this invisible wealth: dark matter. In theoretical physics, dark matter is the stuff in the universe that we can identify only by its gravitational pull. For the Harvard economists, dark matter is foreign wealth, the existence of which we can infer from the income it provides.

How much of it is out there? You can calculate a price for an asset from the earnings it provides. Messrs Hausmann and Sturzenegger elect to value America's net foreign assets at 20 times their annual earnings, which corresponds to a 5% rate of return. Valued at this ratio, America's national “portfolio” of foreign assets and liabilities is really

worth $724 billion, not minus $2.5 trillion. What is more, if its foreign assets are as stable as the authors say, it follows that “the country has not been running a deficit.”

Messrs Hausmann and Sturzenegger were the first to name dark matter, but not the first to discover it. In his book, “The United States as a Debtor Nation”, published last year, William Cline, of the Institute for International Economics, performed the same calculation, backing out the value of America's net foreign assets from the income they generate. (Instead of calling it dark matter, Mr Cline, evidently not a born marketing man, called it “capitalised net capital income”.)

Mr Cline agrees with the dark materialists when they say there is “something misleading about calling a country that makes money on its financial position the world's largest debtor”. But sadly he does not think Americans can stop worrying. After making $36.2 billion in 2004, America made just $4 billion on its net foreign assets in the first three quarters of 2005. If it continues on its present trajectory, it will shell out about $190 billion in 2010, Mr Cline calculates. Using Messrs Hausmann and Sturzenegger's methodology, America's net foreign assets would then amount to minus $3.8 trillion. A dark matter indeed.

Ptaking on Ptolemy

Apart from its name, the dark matter thesis appeals because of its simplicity. Philip Lane, of Trinity College, Dublin, thinks it too simple. It matters, he says, what a nation's foreign wealth is composed of. Foreigners hold a lot of American debt (bonds and bank loans), whereas America holds a lot of foreign equity, especially foreign direct investment (FDI). This has two implications. First, what America pays to foreign creditors depends a lot on interest rates, which have been unusually low in recent years. Second, the value of America's assets depends on the risks they carry. Yet Messrs Hausmann and Sturzenegger apply the same valuation ratio indiscriminately to bonds, equities, trade credits and bank loans on both sides of the balance sheet.

That said, there remains a big gap in reported profitability between American FDI and FDI in America that risk alone cannot explain. Perhaps taxes can. To dodge the revenuemen, a multinational company might report artificially high profits in a low-tax jurisdiction abroad. This tax arbitrage, Mr Lane points out, can shift money from one line of the current account to another. But it does not change the size of the deficit one jot.

To Messrs Hausmann and Sturzenegger, mainstream attempts to explain away dark matter look a bit desperate. Fond of their cosmological analogies, they liken them to the labours of medieval astronomers, trying to fit anomalous movements of the planets into their Ptolemaic model of the universe.

But the authors' thesis raises anomalies of its own. By their own account, dark matter should be stable. It stems from abiding features of the American economy, such as managerial know-how, a prized but uncounted commodity that Americans export to their subsidiaries abroad. But as Ed McKelvey, of Goldman Sachs, points out, America's exports of dark matter seem to jump up and down wildly from year to year: $351 billion in 2004, $1.2 trillion in 2003, just $172 billion in 2002. Dark matter seems to fluctuate at frequencies that are not structural, nor even cyclical. Perhaps they are best described as epicyclical.

Not all physicists regard dark matter as an elegant theoretical solution to the mysteries of the universe. Many think it is a bit of a fudge. Just a few months before the concept was introduced into economics, two theorists were hoping to dispel it from physics. Physicists, you see, expect beauty as well as truth from their theories. Economists, alas, must settle for one or the other.

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* “US and Global Imbalances: Can Dark Matter Prevent a Big Bang?” Short and long versions of the argument are available at www.utdt.edu/~fsturzen/Publications.htm

†For critical commentary see www.rgemonitor.com/blog/setser/113810

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Diet and the unborn child

The omega point

Jan 19th 2006
From The Economist print edition

Getty Images

Omega-3 fatty acids are a crucial component of a healthy diet—particularly, it seems, for pregnant women wanting bright, sociable children

THERE is an old joke that goes, “I'm on a seafood diet—I see food and I eat it.” Sadly, these days, the average see-food diet doesn't include enough seafood, even though fish are a good source of a group of nutrients known as omega-3 fatty acids.

It has been known for some time that omega-3 acids are important, but data from a long-term study of British children suggest they are even more important than had previously been realised. In particular, the amount of omega-3 in a pregnant woman's diet helps to determine her child's intelligence, fine-motor skills (such as the ability to manipulate small objects, and hand-eye co-ordination) and also propensity to anti-social behaviour.

That, at least, is the conclusion of Joseph Hibbeln, a researcher at America's National Institutes of Health who has been working with a set of data from the Avon Longitudinal Study of Parents and Children. The Avon study was begun 15 years ago by Jean Golding, of the University of Bristol, with the aim of unravelling the genetic and environmental pathways that predispose children to disease. It contains data on 14,000 expectant mothers and their offspring.

Dr Hibbeln and Dr Golding have been examining this data bank for the effects of maternal nutrition—in particular, the effects of omega-3 intake. Dr Hibbeln announced their conclusions on January 17th at a scientific meeting organised in London by the Institute of Brain Chemistry and Human Nutrition.

Perhaps the most startling finding was that the children of those women who had consumed the smallest amounts of omega-3 fatty acids during their pregnancies had verbal IQs six points lower than average. That may not sound much, but it would have a serious effect on a country's brainpower if it were widespread. And the finding is particularly pertinent because existing dietary advice to pregnant women, at least in America, is that they should limit their consumption of seafood in order to avoid exposing their fetuses to trace amounts of brain-damaging methyl mercury. Ironically, that means they avoid one of the richest sources of omega-3s.

Dr Hibbeln, however, says his work shows that the benefits of eating such fish vastly outweigh the risks from the mercury in them. Indeed, in the Avon study, it was those children exposed to the lowest levels of methyl mercury who were at greatest risk of having low verbal IQ.

The researchers' second finding was that at 3½ years of age, those children with the best measures of fine-motor performance were the ones whose mothers had had the highest intake of omega-3s. Their third finding was that a low intake of omega-3s during pregnancy led to higher levels of pathological social interactions such as an inability to make friends as a child grew up.

Dr Hibbeln said that the “frightening data” showed how 14% of those seven-year-olds whose mothers had had the lowest intake of omega-3s during pregnancy demonstrated such behaviour, compared with 8% of those born to the highest-intake group. This is particularly worrying in the light of work which shows that pathological behaviour in childhood is a good predictor of a lifetime of aberrant behaviour.

Some caution is needed. Studies such as this one, which rely on correlating one variable with another, are not enough to draw firm conclusions on their own, since correlation is not necessarily causation. But these results are supported by several lines of data. One is that the graphs show “dose response” curves—in other words, different levels of omega-3s have different effects. There is also a lot of experimental work showing that omega-3s have behavioural effects on adults. One of Dr Hibbeln's other studies, for example, showed that omega-3 supplements given to violent alcoholics reduced their anger levels by a third within three months.

It also helps to have a plausible mechanism, and Dr Hibbeln thinks there is one. Research published in 2000 by a group in Canada showed that giving omega-3 supplements to piglets doubled the levels of molecules called serotonin and dopamine in the frontal cortexes of the animals' brains. One of serotonin's jobs is to show growing nerve cells how they should connect from the frontal cortex, where reasoning takes place, to the limbic system, the seat of many emotional responses. That is, at the least, suggestive.

Six of the worst

Dr Hibbeln's study concentrated on omega-3 intake directly. But there is a second way that its level might be reduced—by competition with a similar group of fatty acids called omega-6s. Indeed, it may be the ratio of omega-3 to omega-6 in the membranes of cells—particularly nerve cells—which is at the root of the problem, since this can affect the ability of messenger molecules to pass through the membrane. The average cell membrane of an American, whose diet is low in fish and high in omega-6-rich vegetable oils, contains 20% omega-3-based lipids and 80% omega-6-based ones. (Some 10% of American calories now come from linoleic acid in maize and soya oils, the principal sources of omega-6s.) In a Japanese cell membrane, by contrast, the figures are 40% and 60% respectively. The upshot is that Japanese-type cells may be a lot more sensitive to messenger molecules than American-type cells.

The wider social ramifications of such results are unknown, but they may not be negligible. For instance, two reports published by British charities earlier this week, one from the Mental Health Foundation and the other from Sustain, a group that campaigns for better food, claim that changes in diet over the past 50 years—particularly changes in omega-3 and omega-6 consumption—are an important factor behind the rise in mental ill-health in Britain. An old proverb suggests that you are what you eat. If Dr Hibbeln and Dr Golding are right it seems you act what you eat, too.

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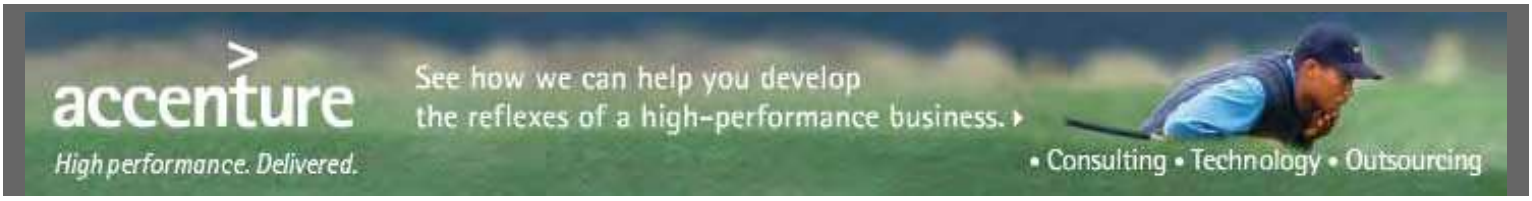
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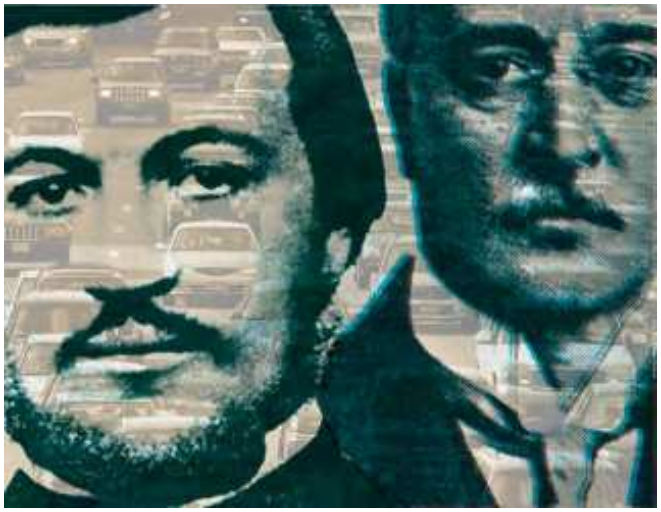
Alternatives to petrol

Gentlemen, start your engines

Jan 19th 2006 | DETROIT
From The Economist print edition



Hybrid motors may not be all they have been cracked up to be, but America's motorists do seem interested in more fuel-efficient cars

VISITORS to the Detroit Auto Show this week will have seen some unusual presentations alongside the regular razzmatazz of concept cars and new models. With America distraught about the security of its oil supplies, and petrol prices stuck well over $2 a gallon (more than 50 cents a litre) for the past year, the once-neglected term “fuel economy” has re-entered the country's vocabulary. It is not, however, an American firm that has led the change. Instead, Toyota, a Japanese company, has made itself the market leader, with its fuel-sipping petrol-electric hybrid, the Prius.

Petrol-electric hybrids attain their fuel economy by using electric motors in stop-start city traffic and petrol engines when cruising on the highway. Toyota expects to sell 400,000 hybrids this year, and the Prius itself now has a waiting list of 18 months. In the wake of this success, every carmaker in the world seems to be touting an alternative to the petrol-driven, four-stroke engine invented by Nikolaus Otto (above left) that has dominated motoring for almost 100 years.

Otto's lotto

In America, that dominion is still overwhelming. Around 97% of cars sold there today rely solely on the pistons, spark-plugs and cylinders of conventional petrol engines to power them (compared with about 50% in Europe). But petrol-electric hybrids, modern versions of the alternative internal-combustion engine developed by Otto's rival, Rudolf Diesel (to the right-hand side of the picture), and even ethanol-burning engines are making inroads. Ford, for instance, aims to sell more than 250,000 hybrid versions of five of its mainstream models this year.

The driving force behind this is hybrids' supposed offer of up to 25% better fuel economy. Although hybrids cost $2,000-3,000 more to buy, the federal government gives tax incentives of up to $3,600 a vehicle for buyers of Priuses and seven other sorts of hybrid made by Toyota, Honda and Ford. On top of this, there are non-monetary inducements, such as the hybrid driver's right to use high-occupancy vehicle lanes on dual carriageways, even when he is alone (and even though this adds to petrol consumption per passenger mile). Equally perversely, this waiver fails to take advantage of the particular benefits of hybrids, which are built for stop-go traffic where braking

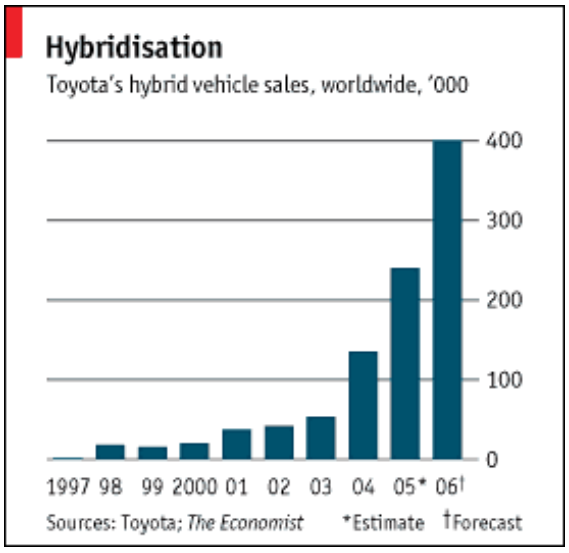
recharges the battery and boosts fuel economy.

Indeed, research has been picking other holes in the hybrid story over the past two years. *Consumer Reports*, a product-rating publication, tested 303 vehicles in real-life town and highway driving, and found that nine out of ten of them failed to achieve the fuel-efficiency claimed for them in tests by America's Environmental Protection Agency (EPA). In some cases the shortfall was as high as 50% and the worst offenders were the hybrids. To the silent glee of Detroit's manufacturers, who were slow off the mark with hybrids, the EPA is about to revise the way it conducts its measurements. The likely outcome is that hybrids (with Toyota and Honda to the fore) will fare far worse.

Only a cynic would suggest that domestic manufacturers had encouraged this updating of fuel-economy standards—for there is indeed a case for modernising tests last revised in 1985. Since then, congestion has grown worse, energy-demanding air conditioning has become routine, and highway speed limits have risen from the 55mph that was enforced after the oil shock of 1973-74. Hybrids, then, may have been oversold. But they are not the only answer to the fuel-economy question.

Rudolf to the rescue

One effect of the 1970s oil shock was to encourage people to buy cars with diesel engines, which are usually more efficient than Otto-cycle engines. However, the fashion did not last. Diesels disappeared from American cars in the 1980s because they were dirty, dull and unreliable.



Two things, however, are reviving interest in them. One is the appearance of cleaner, low-sulphur fuel. This is already commonplace in Japan and Europe, and will be introduced to America in the autumn. It contains a mere 15 parts per million of sulphur, which is less than a thirtieth of the amount tolerated today. Coupled with recent advances in direct injection ("common rail") engines that improve combustion, and durable particulate traps to capture tiny but dangerous particles of soot, this new fuel is cleaning up emissions and transforming the prospects for diesels in America. J.D. Power, a market research firm, forecasts that the share of the market taken by diesel cars will quadruple from today's 3.2% by 2015.

At the motor show, Mercedes-Benz, Honda, BMW, Nissan and Chrysler all revealed their intentions to make diesel engines available in their American cars. Volkswagen, which sold about 30,000 diesels in America last year, says it could have flogged twice that number if it had anticipated the rise in demand. Mercedes is promoting its new BLUETEC system—which incorporates oxidising catalytic converters, particulate filters and a new nitrogen-oxide-reducing system that injects the fuel with urea. This chemical grabs oxygen atoms from nitrogen oxides to produce nitrogen gas (which is harmless) and water. BLUETEC will thus meet new, tougher federal rules on nitrogen-oxide pollution that come into force in 2009. Mercedes claims the new diesel engines it intends to put on the American market will also be 20-40% more economical than their petrol equivalents. It quotes estimates by the Department of Energy which say that if only one-third of America's cars and light trucks were diesels, this would save a quantity of oil equivalent to the country's imports from Saudi Arabia.

Coal-powered cars

Dieter Zetsche, the chief executive of DaimlerChrysler, Mercedes' owner, is still awaiting formal approval from the authorities for his company's new system. He believes, however, that he has satisfied concerns from the EPA that drivers would not bother to top up the urea-injection system, and that the cars would thus pollute more than they should. He thinks diesels are about to take off as smartly as hybrids did. Others beg to differ. GM reckons it is wiser to spend its research budget on technologies such as “lean-burn” petrol engines than to try to make diesels cleaner. Lean-burn engines use a trick called homogenous charge-compression ignition—in effect, they are petrol-burning diesels, since they use pressure rather than spark plugs to ignite the mix of air and fuel. By copying a diesel's operating cycle they obtain a similarly superior thermal efficiency and, hence, fuel economy.

And those who don't like diesels can take other paths to clean and economical cars. The latest buzz is around “plug-in” hybrids. These are vehicles with even smaller than usual petrol engines, bigger batteries and the ability to recharge from the mains overnight. Given that the average American motorist travels barely 30 miles (50km) a day, the petrol engine in such a hybrid is there mainly to stop the driver being stranded by a flat battery.

Supporters of plug-ins, such as James Woolsey, a former head of America's Central Intelligence Agency and a man obsessed with the country's energy security, think such cars offer a clever answer to dependence on petrol. By shifting the donkeywork of supplying energy for transport to power stations—which generally burn coal—they make drivers less vulnerable to the vagaries of the petroleum trade.

Carmakers, though, are sceptical about plug-ins. Publicly, they claim the batteries will not tolerate the rugged regime of recharging envisaged by Mr Woolsey and his fellow enthusiasts. Some people, however, suspect that the real reason for the scepticism is a worry that the successful marketing message which has launched the Prius and its rivals might be tarnished by memories of plug-in electric vehicles, such as General Motors' EV1, which flopped in the 1990s.

If plug-ins fail to catch on, another way of escaping the Middle East would be to burn ethanol made from crops. A blend of 85% ethanol with 15% petrol, known as E85, is gaining acceptance since it can be used in normal petrol engines, and advances in biotechnology promise cheaper ethanol by turning waste cellulose into the glucose from which ethanol is fermented. (At the moment most of it comes from maize seeds.) If that works, it would put paid to the old objection that “gasohol”, as it is sometimes known, consumes more energy in the making than it releases in the engine. Further down the road, companies such as Ford and BMW see great possibilities for burning hydrogen in internal combustion engines (long before it is common in fuel-cell electric cars). And then there are fuel cells themselves—though they are still some way off. In the race to find alternatives to petroleum, the contenders are already on the grid.

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Malaria

A pre-emptive strike

Jan 19th 2006
From The Economist print edition

A plan to stop the evolution of resistance to a new malaria drug

Get article background

THERE is no better example of natural selection in action than the evolution of drug resistance. As night follows day, drugs against infectious micro-organisms are developed, made available to doctors, deployed successfully for a few years, and then become less and less effective as genes for resistance spread through the enemy population. This time, though, it will be different—at least, if the World Health Organisation has its way.

The WHO's particular concern is artemesinin, a newish drug against malaria that cures 95% of those who take it. Arata Kochi, the recently appointed head of the WHO's malaria department, would like to keep things that way.

Dr Kochi's fear is that too much artemesinin is being taken by itself as a so-called monotherapy, rather than in combination with other drugs. That matters for two reasons. First, punching a bug with two drugs simultaneously produces a bigger effect. In combination with something else, artemesinin cures in about three days; alone, it takes seven. The second reason is that if a drug is administered by itself, the bug can evolve resistance more easily. Two drugs mean that mutations protective against both have to happen simultaneously for a resistant strain to emerge.

Unfortunately, when drugs are combined into a single pill, the mixture has to be approved by the authorities, with all the time and expense of clinical trials that involves. Only one such combination has been given the go-ahead so far. In the interim, the WHO wants drug companies to “co-blister” pills made of suitable drugs into a single pack. Not all firms are keen, though. Monotherapies are cheaper to make, particularly as they often come as five-day courses rather than the seven needed for maximum efficacy. Also, sufferers who have heard that artemesinin is a wonder drug may not understand the need for combination therapies.

The WHO has persuaded many poor-country governments that their health services should use only combination therapies, but that does not normally apply to commercial sales from pharmacies, so the agency has just published a list naming and shaming firms (mostly Chinese) that sell monotherapies. Whether its lofty disapproval will persuade manufacturers to change their ways remains to be seen. But if it does not, artemesinin risks going the way of its predecessors.

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Economist.com BOOKS & ARTS

New Orleans jazz

Jelly on a roll

Jan 19th 2006
From The Economist print edition

A re-release of a pre-war jazz recording is flying off the shelves

Getty Images

IN 1938, a casual encounter in Washington, DC, inspired one of the most remarkable documents in American music and culture. Alan Lomax, the young director of the American Archive of Folk Song at the Library of Congress, heard that Jelly Roll Morton, a legendary pianist-composer from the bygone days of New Orleans jazz, was languishing in a seedy local club. Renowned as much for his bravado as his talent (his very nickname was a shameless sexual boast), Morton bitterly resented being cast aside by the flashy big bands of the swing era and was keen to stake his rightful claim to recognition.

Though Lomax actually disliked jazz, considering it a corruption of folk-music purity, he invited Morton to the Library of Congress to record some of his New Orleans memories. The moment the veteran pianist began to talk, play and sing, Lomax realised he had struck gold. That one-off interview stretched into months, producing a unique portrait of a fabulous time and place, mesmerisingly evoked by a Creole genius.

Despite their value and status among connoisseurs, the Jelly Roll Morton Library of Congress recordings have had a chequered history. A commercial edition was only released in the 1950s, with cuts and primitive sound. Subsequent versions were similarly truncated, at the cost of either music or speech and the loss of the spontaneous continuity between them, as Morton interweaves memories, pronouncements and performance. But at long last, the whole set has appeared in its glorious nine-hour entirety, on the Rounder Records label, presented in a handsome, piano-shaped box. It contains the sessions on seven CDs with an additional one devoted to Lomax's interviews with some of Morton's New Orleans contemporaries. Also included are a copy of Lomax's biography, “Mr Jelly Roll”, based on the Morton interviews, and a comprehensive essay by John Szwed, a jazz scholar, setting the whole project in context.

So fans of jazz, music in general, or just the incomparable richness of the human scene can relish Morton's musings complete, in state-of-the-art sound. Softly strumming the keys like a singer of tales, he recalls the “tough

babies and sweet mamas” of the fabled red-light district of Storyville, and such denizens as Sheep Bite, Toodlum Parker and Chicken Dick. He conjures up a New Orleans funeral, from the wailing dirge to the graveyard to the raucous march back to the wake, with all its sorrow and jubilation—in his words, “the end of a perfect death”.

Every track offers marvels of piano virtuosity, in a whole spectrum of styles. Morton plays Scott Joplin's “Maple Leaf Rag” in brilliant ragtime, then interprets it his own way, slower, but with much more swing. Throughout, he uses these sessions as a platform to demonstrate his views on jazz—not loud and blaring in the modern style, but subtle and melodious, with an irresistible beat and ample scope for dynamics and imagination.

Everything he plays embodies those qualities—a captivating exploration of “Tiger Rag”, going back to its ballroom origins as a quadrille, an utterly infectious tune called “Salty Dog” which consists of just four chords and a one-note melody, or a party piece like “Animule Ball”, an exuberant display of Morton the master entertainer, comprising jokes, freewheeling singing, and the scintillating keyboard touch which raised him above his rivals.

In the short time since it appeared, this magnificent boxed set has been flying off the shelves. With music and personality of such timeless appeal, this is no surprise. Of course, Morton would regard it as simple vindication of the supremacy he always claimed, and about time too. But it is also a monument to the vision, skill and commitment of Alan Lomax. His encounter with the New Orleans master was one of the key moments in a life devoted to bringing the riches of folk and vernacular music to as wide an audience as possible.

Pre-Morton, Lomax had concentrated on field work in the American South, gathering songs from local musicians. But the Library of Congress interviews with Morton suggested a whole new realm of possibility, not just focusing on musical materials but bringing to life the very cultures which they expressed and embodied. As Lomax put it, “I later came to call this process ‘the cultural feedback system', where people talk their images into a recording instrument or into a film, and suddenly begin to find that they have importance. All that came out of the Jelly Roll interview...This was the first oral history. Jelly Roll invented oral history, you might say.”

Over a long life—he died in 2002 at 87—Lomax pursued his belief in what he called “cultural equity” over a huge range of projects: the extensive Lomax collection on Rounder Records encompasses Italy and Ireland, American prisons, the Caribbean and much more. It all reflects Lomax's determination, in his words, “to put sound technology at the disposal of ‘The Folk', to bring channels of communication to all sorts of artists and areas”. While Jelly Roll Morton might jib at being merely classed as one of “The Folk”, he would certainly applaud Lomax's homage to the unique world in which he played such a magnificent part.

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Hunting Osama bin Laden

Notable bilge

Jan 19th 2006
From The Economist print edition

AMERICA attacked Afghanistan in late 2001 with two aims: to obliterate the Taliban regime and the al-Qaeda camps it was harbouring, and to kill the terrorist group's leaders. The first was a cinch. In less than two months, the Taliban and the camps were bombed to bits. But Osama bin Laden and his right-hand man, Ayman al-Zawahiri, are still missing, presumed alive; on January 13th America made its latest failed bid to kill the latter in a provocative air raid on northern Pakistan.

It has previously been journalists and Democratic politicians who groused at this failure. America, they claimed, had Osama bin Laden in its crosshairs at Tora Bora, a honeycomb of lofty caves near the border with Pakistan. Its reluctance to pitch ground-troops into the fight enabled him to escape. In reply, senior American officials, including General Tommy Franks, who commanded the Afghan campaign, have said that it was not known whether Mr bin Laden was at Tora Bora and, moreover, that many American troops were unnecessary as an Afghan militia had been hired to fight in their place.

Not true, says Gary Berntsen, the CIA officer who masterminded the Tora Bora attack. He claims that one of his Arab-American officers listened to Mr bin Laden rallying his troops over the radio of a dead al-Qaeda fighter. And that, given the incompetence and duplicity of his Afghan hirelings, Mr Berntsen in vain requested 800 American army rangers to prevent Mr bin Laden's escape. Of General Franks's claim to the contrary, he writes, he “was either badly misinformed by his own people or blinded by the fog of war.”

Mr Berntsen is understandably annoyed. He seems to have done a remarkable and risky job pushing CIA air-strike controllers high into Tora Bora at a time when the army—though it had not lost a single soldier to enemy fire—refused to send even special forces troops there. Less acceptable is the self-love and ignorance Mr Berntsen exhibits throughout this important yet awful book. His description of Nairobi, to which CIA officers flocked after a 1998 al-Qaeda attack, is erroneous. Bantu denotes an African linguistic group, not a tribe; the language of Afghanistan's biggest group is Pushtu, not Pashtun; Wahhabism, not Wahhanism, is an extremist Islamic movement.

And then there is the writing. Barely a sentence is left unsullied by hackneyed-heroic bilge. Of General Franks's transport plane, he remarks: “I am big; I am bad; and I will kick anyone's ass that I so choose.” His joy at America's meaner weapons is ejaculatory, and, in the slaughter of thousands of Taliban recruits, unsavoury. Of course, Hollywood, for whom this book was presumably written, may not care.

Jawbreaker: The Attack on Bin Laden and Al Qaeda—A Personal Account by the CIA's Key Field Commander.
By Gary Berntsen and Ralph Pezzullo.
Crown; 328 pages; $25.95

Jawbreaker: The Attack on Bin Laden and Al Qaeda—A Personal Account by the CIA's Key Field Commander
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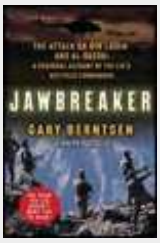

Crown; 328 pages; $25.95

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Economist.com BOOKS & ARTS

Art and artists

Empress of the avant-garde

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KATHARINE KUH'S memoirs, published 11 years after her death, offer a first-hand account of all the anxiety and excitement that went into seeing, showing and making modern art in the second half of the 20th century.

A pioneering art dealer, curator and critic, who witnessed at first-hand the arrival of Modernism in America, Kuh knew everyone who was anyone in the art world at the time. Her first professor was Alfred Barr, the legendary founding director of the Museum of Modern Art (MoMA) in New York. Ludwig Mies van der Rohe, Joseph Albers, Constantin Brancusi, Edward Hopper, Mark Rothko and Clyfford Still all became close friends and confided in her. So attuned was she to their hopes and ambitions that her recollections make her into something of a 20th-century Giorgio Vasari.

My Love Affair with Modern Art: Behind the Scenes with a Legendary Curator
By Katharine Kuh

Edited by Avis Berman. Arcade Publishing; 314 pages; $27.50

Buy it at
Amazon.com
Amazon.co.uk

Kuh was born, according to a preface by Avis Berman, into a well-to-do Jewish family from St Louis—but soon faced adversity when she caught polio. For years Kuh was forced to wear an unwieldy body brace and undergo gruelling daily sessions of physiotherapy. Her father compensated for her isolation as a sick, only child by introducing her to art and teaching her to catalogue his collection of Old Master prints. Kuh's mother, an early feminist, was concerned that her partly disabled daughter should have a proper education and a profession, and she encouraged her to attend Vassar College. Once she had recovered enough to be able to walk—she would limp all her life—Kuh threw herself into everything with a furious energy.

Her short marriage to a Chicago businessman, George Kuh, ended in divorce, and she resolved to spend the rest of her life surrounded by art and the people who made it. In 1935 Kuh opened the first avant-garde gallery in Chicago. There was no market for modern art at the time, but Kuh had the foresight to befriend and exhibit many radical artists, including Albers, Laszlo Moholy-Nagy, Wassily Kandinsky, Isamu Noguchi and Stuart Davis, as well as photographers such as Ansel Adams and Edward Weston. To earn money, she taught art history and after she closed her gallery in 1943 she joined the Art Institute of Chicago, eventually rising to become its first female curator. Kuh worked there for 16 years under its dynamic director, Daniel Catton Rich, who became her long-term lover. Together they organised landmark shows, including the first major Van Gogh exhibition in America, which they arranged in 1948. She went on to curate the American painting show at the Venice Biennale in 1956, although Rich, Ms Berman says, received the credit; at the time, there was no precedent for a woman running the show.

Shortly before she died, Kuh began writing her memoirs. Ms Berman completed the task. Among Kuh's happiest memories, she wrote, were the months she spent working with Van Gogh's nephew, Vincent Willem, when they were planning the famous Post-Impressionist's exhibition. Not only had Willem kept the family collection of over 200 paintings and 500 drawings intact—though he was forced to trade one for provisions during the second world war, when he was hiding a Jewish family and his own family was starving—he also toured it around the world, keeping his uncle's renown alive until the Dutch government built the Van Gogh Museum in 1973.

Kuh's descriptions of her friendships with artists, Rothko in particular, are among the most moving in the book. She describes this troubled genius as a tragic hero, at once obsessed with his own art and insecure about other peoples' opinions of it; completely uncompromising as an artist and yet, even when he was rich and famous, plagued by worries about his financial security and future reputation. She was full of admiration for Rothko's paintings from the 1950s—“those radiant, life-giving canvases electrified by pulsating color mutations”—but

watched helplessly as this once pugnacious painter gravitated towards darkness and ultimately suicide nine years after he had attained what had seemed then to be his life's aspiration: a retrospective at MoMA. “It was never lack of ambition that defeated Mark but the physical limitations of paint and brush. He set himself an impossible task and then grieved when he couldn't force canvas and paint to embrace the whole of life,” she writes.

According to Kuh, Rothko claimed an artistic kinship with Rembrandt, believing that they both sought what he called “a maximum of poignancy”. On the surface it is difficult to imagine two more different painters, but both poured their lives into their art and had the rare ability to connect to the human spirit. Katharine Kuh believed this was the key to great art. Luckily, she devoted her life to sharing it with others.

My Love Affair with Modern Art: Behind the Scenes with a Legendary Curator.
By Katharine Kuh.
Edited by Avis Berman. Arcade Publishing; 314 pages; $27.50

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Renaissance science

The uses of enchantment

Jan 19th 2006
From The Economist print edition

PARACELSUS, or Philip Theophrastus Bombastus von Hohenheim, is one of the oddest and most intriguing figures of late medieval European history. Part doctor, part alchemist, theologian and prolific writer, he was also a querulous braggart who fell out regularly with his patrons, antagonising those who tried to help him, which may explain why he never stayed in one place for long.

Born in Switzerland in 1493, a year after Christopher Columbus journeyed to the New World, Paracelsus travelled all over Europe, from the Arctic Circle to the Black Sea, healing the sick, preaching, occasionally teaching in universities and all the time writing books, almanacs and pamphlets. Many of the places he visited had been touched by the bubonic plague that swept Europe in the 15th and 16th centuries, and he was fascinated by the legend of the four horsemen of the apocalypse. He was a great humanist who spent much of his time reading Plato and Aristotle. A self-taught expert on mining, he is often regarded as one of the fathers of modern chemistry, yet chemists don't always know what to make of him and are embarrassed by his rantings.

Nevertheless, Paracelsus is an important contemporary of Nicholas Copernicus, Martin Luther, Leonardo da Vinci and the other figures commonly associated with the transformation of medieval ideas about philosophy, medicine, politics and religion. And he remains an inspiration to those interested in untangling the roots of modern science, when magic was important both to ordinary people and to the evolution of scientific knowledge.

The Devil's Doctor: Paracelsus and the Renaissance World of Magic and Science
By Philip Ball

To be published in America by Farrar, Straus and Giroux in April
William Heinemann; 430 pages; £20.

Buy it at
Amazon.com
Amazon.co.uk

Poets have always loved him. Paracelsus was said to travel on a white horse and to carry the elixir of life in the pommel of his broadsword. Goethe and Thomas Mann both used him as a model for their versions of Faust; he appears in novels by Jeanette Winterson and A.S. Byatt, and there is a bust of him near the common room of Harry Potter's house at Hogwarts School of Witchcraft and Wizardry.

Despite his hold on the modern imagination, the true Paracelsus remains difficult to separate from the myth that grew up around him. His writings are scattered in libraries all over the world. Even when physically available, they are never easy to understand. Though occasionally he wrote in Latin, Paracelsus liked also to use a Low German that was full of unusual, little-known words. The University of Zurich has undertaken to collect and catalogue his writings in a vast programme known as the Zurich Paracelsus Project. Progress is slow, though, and work on the Paracelsus Dictionary has reached only the letter B.

Philip Ball, who is a scientist rather than a historian, has chosen to take on the challenge of explaining Paracelsus by offering as much context as he can find. Given that Paracelsus lived during one of the most turbulent periods of European history—in the early part of the Counter-Reformation and just before the Thirty Years War—this was not an unreasonable decision. However, faced with such a mountain of historical material, the clarity that characterised Mr Ball's “Critical Mass”, winner of the Aventis science book prize last year, has deserted him on this occasion. No sooner does Paracelsus move at the age of nine to the Carinthian mountains in Austria, for example, than Mr Ball takes a detour into the history of mining; a description of Paracelsus's education offers an excursion into the background of humanism, ancient cures, Galen and the early history of dissecting; a short commentary on Paracelsus's pacifism and his religious philosophy turns into a study of the Anabaptist rebellions; an exploration of the problems facing the Roman Catholic Church leads into an analysis of how Luther might have been affected by being constipated. All this before you reach page 150.

Mr Ball's enthusiasm for the wider picture is to be admired, but somewhere in all this Paracelsus is lost. The book is full of wonderful nuggets, but the thread of ideas is difficult to follow. This may be his first “life and times” for 40 years. But with far more “times” than “life”, the balance between the two is not wholly successful.

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Economist.com BOOKS & ARTS

American drought

Unforgiving land

Jan 19th 2006
From The Economist print edition

ONE of America's worst environmental disasters, according to this moving and lyrical book, was the Dust Bowl of the 1930s. In parts of the Great Plains, cows produced “chocolate milk”, the result of dust being mixed up with the real stuff. Chickens choked on dust. Children died of dust pneumonia.

The trouble began, Timothy Egan explains, in the early 1900s. Homesteading whites on their way west saw inviting grassland, and pushed both Indians and bison off it. They settled in marginal areas “when there was no other land left to take.” The native vegetation was ripped up as the newcomers planted wheat, lots of it. As prices rose during the 1920s, people and their ploughs kept on coming.

At the same time the weather grew worse. Rain had been plentiful in the 1920s, but then it stopped. Wheat prices collapsed from over-supply, at just about the time that the Depression hit. And the land, unanchored by grass, began to blow away. For years, it literally rained dust. Up to 100m acres of land was devastated. The largest storm of all, on April 14th 1935 (“Black Sunday”), dumped enough dirt to fill the Panama Canal twice over.

If this sounds far-fetched, take a look at the remarkable photographs in this book. The cover shows a malignant yellow-brown cloud churning towards hapless dwellings on the Kansas prairie. Other black-and-white images include a house nearly buried by dust dunes and a “black blizzard” overtaking a Model-T Ford. The dust storms—sometimes as many as 100 a year—scraped people's skin “like steel wool”. Dust from the mid-west even blotted out the sun for a few days in New York and Washington, DC. (“There goes Oklahoma,” puzzled senators were told.)

Mr Egan, a *New York Times* reporter, has interviewed many survivors for his project, and a spirited cast of characters emerges. There was “Alfalfa Bill”, the governor of Oklahoma, who thought his homeland could become a garden. John McCarty, an even more delusional local newspaper editor, founded the Last Man's Club for people who planned to stick it out as a matter of pride. He left in 1936. A saviour of sorts was Franklin Roosevelt, who fought erosion by planting trees. FDR's henchmen also convinced sceptical farmers to create soil-conservation districts.

Eventually, the rains came back (though probably not thanks to local efforts to explode the clouds by firing rockets at them). Water from an aquifer, as well as better conservation, has since kept the soil in place even during dry years—though this month, the same land, bone-dry once again, has been swept with dangerous fires. As Mr Egan acridly points out, one legacy of those terrible times still endures. Farm subsidies got their start during the Dust Bowl; they were meant for people whose dying animals had stomachs full of dirt. Today, huge agribusinesses and their powerful congressional allies have kept the subsidies flowing. That is no way to honour the hardships of the 1930s.

The Worst Hard Time: The Untold Story of Those Who Survived the Great American Dust Bowl.
By Timothy Egan.
Houghton Mifflin; 340 pages; $28

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American reflections

French letters

Jan 19th 2006
From The Economist print edition

SAY what you like about the French; you never know what to expect when they write about the United States. They have produced by far the best book on the country, Alexis de Tocqueville's “Democracy in America”, as well as a disproportionate share of the worst. They are capable of the most grovelling America-worship as well as the most grotesque anti-Americanism: just try changing the subject on the *rive gauche* from the evils of George Bush to the wonders of Woody Allen.

All of which adds to the suspense about Bernard-Henry Lévy's new book, “American Vertigo”. Mr Lévy is a quintessential French intellectual—a “superman and a prophet”, at least according to *Vanity Fair* magazine. Mr Lévy recently spent a year travelling around the United States in de Tocqueville's footsteps, courtesy of a clever (and extremely generous) commission from *Atlantic Monthly*. The result is a strange product—more a collection of notes than a polished manuscript. Mr Lévy never rises to de Tocqueville's heights; indeed, his reflections on the spirit of democracy and equality can be remarkably flat, as when he muses on America's lack of a European-style fast lane on its highways. And he spends far too much time telling us things that we already know—that Buffalo and Detroit are bombed-out wrecks and Los Angeles is a jolly big place where people spend a lot of time in their cars.

American Vertigo: Traveling America in the Footsteps of Tocqueville
By Bernard-Henri Lévy

Random House; 320 pages; $24.95

Buy it at
Amazon.com
Amazon.co.uk

Still, “American Vertigo” is much better than most European books on America at the moment. Mr Lévy visited the country during the 2004 election and managed to meet an astonishing number of interesting people, including Woody Allen, Warren Beatty, John Kerry and Norman Mailer. He is generally sympathetic to his host country, dismissing the charge that America is degenerating into a theocracy and even finding a few kind words for the neoconservatives. But he is acutely aware of the country's oddities—not least its strange commitment to both freedom and order. He is particularly struck by a sign in a San Francisco swingers' club: “No alcohol. No drugs. No sleeping. No uproarious or loud laughter. Condoms obligatory. Turn all cell phones off.”

“American Vertigo” is worth reading for these delicious details; it is doubly worth reading if it sends you back to de Tocqueville's original masterwork.

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By Bernard-Henri Lévy.
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Heinrich Harrer

Jan 19th 2006
From The Economist print edition

Heinrich Harrer, mountaineer and explorer, died on January 7th, aged 93

Keystone

WHEN Heinrich Harrer gazed for the first time on Lhasa, the capital of Tibet, in 1946, he noticed especially the roof-pinnacles of the Potala Palace, gleaming with gold. After 21 months on the run from a British prison camp, having crossed 65 mountain passes and 1,000 miles of territory more than 16,000 feet high, it seemed like a glimpse of Paradise. He had travelled by yak and on foot; he was now verminous and starving, in rags of sheepskin, crippled with sciatica from sleeping on frozen ground, and without a rupee to his name. But gold shone ahead of him.

He little knew that up on that roof, from time to time, a boy of 11 would wander up and down. The youngster had an excellent collection of field glasses and telescopes, and these he would train on the town, watching people. When his subjects—for he was their god, and they his worshippers—realised he was observing them, they would try to remove themselves from his field of vision. But, if only from a distance, the young Dalai Lama would try to catch them. His life otherwise was study and prayer, in dark rooms, with few visitors. The roof was his window on the world.

Tibet at that time was completely closed to foreigners. A foreigner like Mr Harrer—an Austrian mountaineer, fetching up in Lhasa with flowing beard and hair, speaking Tibetan like a peasant—was particularly suspect. But having got there with such effort, he could not bear to leave. Gradually, his life and that of the child-god began to intersect. At religious ceremonies, as the Dalai Lama processed through ecstatic crowds and colonnades of statues made of butter, he would dart sly smiles at Mr Harrer, seeing a figure every bit as exotic as himself.

Mr Harrer, a champion skier and, since his village boyhood, happiest on snow and ice, built a skating rink below the palace. There the Lhasans, delighted and mystified, learned the art of “walking on knives”. The Dalai Lama, who could not see the rink through his telescope, sent a request for a cine-film of the skaters. Then he asked for a cinema. Mr Harrer built him one, running the projector off an old Jeep engine, and discovered at his first proper audience with the living Buddha that the boy had already dismantled and re-assembled it, all by himself.

Over the succeeding months Mr Harrer became his photographer, his teacher and his friend. He taught him maths, geography, science, and what Churchill and Eisenhower had done. As Mr Harrer recorded and slowly understood Tibet, accustoming himself to barley porridge, searing cold and the virtue of stoical patience, the Dalai Lama with avid curiosity pieced the outside world together—until, in 1950, the Chinese invasion of Tibet put an end both to his political innocence and to Mr Harrer's seven-year sojourn there.

They had been, he said later, the happiest years of his life. They had also been unintended. Mr Harrer had gone to Kashmir in 1939 on quite different business, to scout out a “killer mountain” called Nanga Parbat for a possible assault by his team of German and Austrian climbers. He had been arrested instead, on the eve of war.

His purpose in Kashmir had not been entirely unpolitical. He was already a hero in Austria for having made, with three others, the first successful ascent of the infamous north face of the Eiger in 1938. The conquering of the mountain had coincided with Austria's absorption into Nazi Germany, a highly symbolic display of united dominance and strength. Hitler himself had congratulated him. Keyed up by that, Mr Harrer longed to be picked for a Himalayan expedition. To make himself more eligible, he joined the Nazi party and the Styrian SS, and was hired to teach SS officers skiing.

On the White Spider

The Dalai Lama knew nothing of his teacher's past. Mr Harrer did not wish to tell him. He might have told no one, had not the book he wrote of his experiences, “Seven Years in Tibet”, been made in 1997 into a Hollywood epic, with Brad Pitt starring as himself. This drew attention, then investigation. Nothing remotely evil was ever attributed to Mr Harrer; he said he had worn his SS uniform only once, at his wedding.

The witch-hunters ensured that the rest of his life was tainted by this episode. But Mr Harrer's passion was mountains, and it was this passion alone that had ever got him into trouble. The most dangerous moment of his life —the moment after which, he said, he felt privileged to remain alive at all—saw him dangling on the 7,000-foot vertical face of the North Wall of the Eiger, no crampons on his boots, with the surface continually melting in the sun and rocks cascading past him. He was on the White Spider, a network of sheer ice on which nine mountaineers had died not long before. There was no shelter or hiding place; he was continually exposed. And far below, in the meadow from which the mountain rose, a crowd of telescopes was trained on him.

He later said he felt nothing but contempt for those who had observed him, safe and distant, like indifferent gods. He was to feel quite differently about the god, with his long hair and glowing, excited smile, who tried so hard to observe him through his telescope in Lhasa.

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Overview

Jan 19th 2006
From The Economist print edition

Oil jumped and **stockmarkets** fell. A barrel of West Texas Intermediate breached $66 on January 17th, thanks to unruliness in Nigeria and defiance from Iran. Meanwhile, Japan's Nikkei stock index fell by 5.7% at the start of the week, before clawing back 2.7% on January 19th.

America's **consumer prices** fell for the second month in December, by 0.1%, thanks to lower energy costs. Prices remained 3.4% higher than the year before. Its **industrial output** grew by 2.8% in 2005. Production stood at 80.7% of full capacity in December, just below its long-term average.

America attracted a net **capital inflow** of $89.1 billion in November. Its **trade deficit** in goods and services narrowed slightly to $64.2 billion in November, from a record $68.1 billion in October.

Industrial output in the **euro area** expanded by 2.6% in the year to November, led by a 4.1% gain in capital-goods production.

Japan's producer prices rose by 0.2% in December, helped by increases in the price of pork and unwrought copper. This left them 2.2% higher than the year before.

In the three months to November, **Britain's** unemployment rate rose to 5.0%, the highest since 2003. Annual inflation, which peaked at 2.5% in September, fell to 2.0% in December.

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Output, demand and jobs

Jan 19th 2006

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% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2005	2006	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 2.6	Q3	+ 0.6	+ 2.7	+ 3.2	+ 0.7	Q2	+ 1.2	Q3	5.1	Dec	5.1
Austria	+ 1.8	Q3	+ 2.3	+ 1.8	+ 2.0	+ 3.0	Oct	+ 1.3	Oct	5.3	Dec	5.0
Belgium	+ 1.1	Q3	+ 1.7	+ 1.4	+ 1.9	– 7.7	Oct	+ 0.8	Oct	12.9	Dec†	12.8
Britain	+ 1.7	Q3	+ 1.7	+ 1.7	+ 2.1	– 2.4	Nov	+ 2.1	Nov	5.0	Nov††	4.7
Canada	+ 2.8	Q3	+ 3.6	+ 2.9	+ 3.1	+ 1.7	Oct	+ 2.5	Oct	6.5	Dec	7.0
Denmark	+ 4.8	Q3	+ 5.7	+ 3.0	+ 2.8	+ 2.9	Nov	+ 3.5	Nov	5.2	Nov	6.2
France	+ 1.8	Q3	+ 2.8	+ 1.5	+ 1.9	+ 1.3	Nov	+ 0.5	Nov	9.6	Nov	10.0
Germany	+ 1.4	Q3	+ 2.5	+ 1.1	+ 1.7	+ 4.7	Nov	– 0.6	Nov	11.2	Dec§	10.8
Italy	+ 0.1	Q3	+ 1.1	+ 0.2	+ 1.3	+ 0.4	Nov	+ 0.4	Oct	7.5	Sep	7.9
Japan	+ 2.9	Q3	+ 1.0	+ 2.5	+ 2.4	+ 3.4	Nov	+ 0.9	Nov	4.6	Nov	4.6
Netherlands	+ 1.3	Q3	+ 2.5	+ 0.8	+ 1.9	+ 0.4	Nov	+ 3.5	Oct	6.3	Dec**	6.7
Spain	+ 3.5	Q3	+ 3.3	+ 3.4	+ 3.0	+ 0.8	Nov	+ 0.1	Nov	8.5	Nov	10.5
Sweden	+ 3.4	Q3	+ 3.9	+ 2.6	+ 3.1	+ 1.0	Nov	+ 9.0	Nov	5.4	Dec†	5.3
Switzerland	+ 2.3	Q3	+ 4.3	+ 1.8	+ 2.1	+ 2.8	Q3	+ 2.8	Oct	3.8	Dec†	4.0
United States	+ 3.6	Q3	+ 4.1	+ 3.6	+ 3.3	+ 2.8	Dec	+ 4.4	Nov	4.9	Dec	5.4
Euro area	+ 1.6	Q3	+ 2.6	+ 1.4	+ 1.9	+ 2.6	Nov	+ 0.3	Nov	8.3	Nov	8.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 1.9	Q3	+12.1	na	na	– 3.4	Nov	+ 5.1	Nov	8.3	Nov	8.7
Greece	+ 3.8	Q3	na	na	na	+ 0.9	Nov	+ 2.6	Oct	9.7	Q3	10.1
Iceland	+ 4.0	Q3	na	na	na	na		na		1.5	Nov†	2.6
Ireland	+ 4.8	Q3	+ 1.3	na	na	+14.8	Nov	+ 4.3	Oct	4.3	Dec	4.3
Luxembourg	+ 3.1	Q1	na	na	na	+ 3.3	Oct	– 2.9	Nov	4.9	Nov	4.4
New Zealand	+ 2.0	Q3	+ 0.2	na	na	– 2.7	Q3	+ 4.9	Q3	3.4	Q3	3.8
Norway	+ 3.1	Q3	+ 3.2	na	na	+ 1.0	Nov	+ 3.8	Nov	4.6	Nov‡	4.5
Portugal	+ 0.2	Q3	– 3.7	na	na	+ 0.5	Nov	+ 1.1	Nov	7.7	Q3†	6.8

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ††Sep-Nov; claimant count rate 2.9% in Dec. §EU harmonised rate 9.3% in Nov. **Oct-Dec. ‡Sep-Nov.

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WEEKLY INDICATORS

Prices and wages

Jan 19th 2006

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% change on year ago

	Consumer prices		The Economist poll consumer prices forecast		Producer prices		Wages/earnings	
	latest	year ago	2005	2006	latest	year ago	latest	year ago
Australia	+ 3.0 Q3	+ 2.3	+ 2.8	+ 2.9	+ 6.2 Q3	+ 6.1	+ 6.1 Q3	+ 3.5
Austria	+ 1.6 Nov	+ 2.6	+ 2.3	+ 1.9	+ 1.4 Dec	+ 5.2	+ 2.4 Dec	+ 2.0
Belgium	+ 2.9 Dec	+ 2.3	+ 2.5	+ 2.1	+ 1.7 Nov	+ 5.6	+ 2.3 Oct	+ 2.4
Britain	+ 2.0 Dec*	+ 1.6	+ 2.1	+ 2.0	+ 2.4 Dec	+ 2.9	+ 3.4 Nov†	+ 4.3
Canada	+ 2.2 Dec	+ 2.1	+ 2.3	+ 2.3	+ 2.9 Nov	+ 3.8	+ 2.8 Oct	+ 2.0
Denmark	+ 2.2 Dec	+ 1.2	+ 1.8	+ 1.9	+ 4.6 Dec	+ 2.7	+ 2.8 Q3	+ 2.9
France	+ 1.5 Dec	+ 2.1	+ 1.9	+ 1.7	+ 2.8 Nov	+ 3.2	+ 3.2 Q3	+ 2.9
Germany	+ 2.1 Dec	+ 2.1	+ 2.0	+ 1.7	+ 2.4 Dec	+ 3.8	+ 1.0 Oct	+ 2.3
Italy	+ 2.0 Dec	+ 2.0	+ 2.1	+ 2.1	+ 3.7 Nov	+ 4.3	+ 3.0 Nov	+ 2.7
Japan	− 0.8 Nov	+ 0.8	− 0.2	+ 0.3	+ 2.2 Dec	+ 1.9	− 0.3 Nov	+ 3.5
Netherlands	+ 2.0 Dec	+ 1.2	+ 1.5	+ 1.5	+ 4.5 Nov	+ 5.7	+ 1.1 Dec	+ 0.7
Spain	+ 3.7 Dec	+ 3.2	+ 3.4	+ 3.1	+ 4.9 Nov	+ 5.2	+ 1.9 Q3	+ 2.2
Sweden	+ 0.9 Dec	+ 0.4	+ 0.5	+ 1.5	+ 5.0 Nov	+ 2.9	+ 3.1 Oct	+ 3.8
Switzerland	+ 1.0 Dec	+ 1.3	+ 1.2	+ 1.1	+ 1.1 Dec	+ 1.7	+ 0.9 2004	+ 1.4
United States	+ 3.4 Dec	+ 3.3	+ 3.4	+ 2.9	+ 5.7 Dec	+ 4.4	+ 3.1 Dec	+ 2.6
Euro area	+ 2.2 Dec	+ 2.4	+ 2.2	+ 2.0	+ 4.2 Nov	+ 3.7	+ 2.2 Q3	+ 1.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*							
Finland	+ 1.0 Dec	+ 0.4	na	na	+ 5.2 Dec	+ 0.7	+ 3.6 Q3	+ 4.0
Greece	+ 3.6 Dec	+ 3.1	na	na	+ 6.5 Nov	+ 4.0	na	na
Iceland	+ 4.4 Jan	+ 4.0	na	na	+ 3.9 Dec	+ 5.9	+ 7.3 Nov	+ 5.4
Ireland	+ 2.6 Nov	+ 2.9	na	na	+ 3.5 Nov	− 1.6	+ 3.5 Q3	+ 4.7
Luxembourg	+ 2.5 Dec	+ 2.2	na	na	+ 1.9 Nov	+15.6	+ 2.7 Sep	− 0.1
New Zealand	+ 3.2 Q4	+ 2.7	na	na	+ 6.1 Q3	+ 2.5	+ 3.0 Q3	+ 2.2
Norway	+ 1.8 Dec	+ 1.1	na	na	+24.3 Dec	+ 9.7	+ 2.6 Q3	+ 4.3
Portugal	+ 2.6 Dec	+ 2.5	na	na	+ 3.4 Nov	+ 5.2	+ 1.2 Nov	+ 0.5

*RPI inflation rate 2.2% in Dec. †Sep-Nov.

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WEEKLY INDICATORS

Switzerland

Jan 19th 2006

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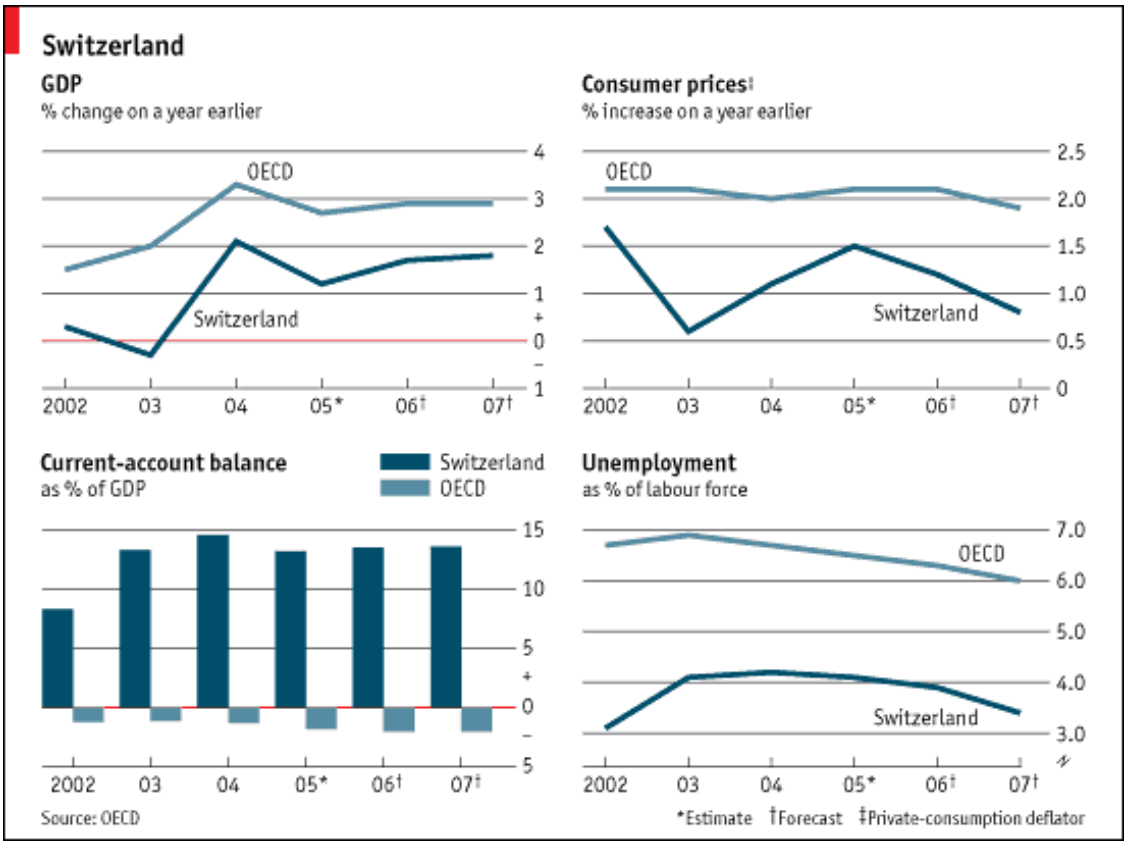

The Swiss remain a prosperous people, but economic growth has been disappointing for many years. Only a mild recovery is in store after the setback in 2005, when GDP rose by little more than 1%. Indeed, the economy is stuck in “a low-growth trap”, says the OECD, chiefly because of weak gains in efficiency. The main reasons why productivity growth has been so sluggish are a lack of competition in sheltered product markets together with a poorly performing public sector. Although Switzerland's record of innovation is among the best, it is weaker in smaller firms and is not being helped by low attendance at university. The OECD recommends reforms to reduce trade protection and to liberalise the postal services and electricity and gas industries. It also calls for more competition in the health system to promote greater efficiency.

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Money and interest rates

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	Money supply* % change on year ago			Interest rates % a year (Jan 18th 2006)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 6.6	+ 8.7	Nov	5.62	5.41	5.10	5.11	5.34	6.19
Britain	+ 5.3	+12.1	Nov	4.53	4.81	4.19	3.94	4.56	5.14
Canada	+ 9.3	+ 8.4	Nov	3.42	2.45	3.75	3.97	4.28	5.23
Denmark	+19.2	+12.2	Nov	2.50	2.25	2.75	3.22	3.63	4.92
Japan	+ 5.5	+ 2.0	Dec	0.03	0.02	0.24	1.43	1.35	1.52
Sweden	+ 2.7	+ 7.2	Nov	1.83	1.99	2.46	3.17	3.62	3.18
Switzerland	+ 5.4	+ 5.6	Dec	0.99	0.73	1.68	1.91	2.07	2.27
United States	- 0.1	+ 7.8	Dec	4.48	2.58	4.34	4.34	4.18	5.31
Euro area†	+10.6	+ 7.6	Nov	2.51	2.08	2.80	3.24	3.49	3.72

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. † Germany for bonds. Benchmarks: US 30-year 4.51%, Japan No. 274 1.43%. Central bank rates: US fed funds 4.25%, ECB refinancing 2.25%, BOJ overnight call 0.001%, BOE repo 4.5%. Sources: Bank of Canada, Commerzbank, Danske Bank, J.P. Morgan Chase, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Jan 19th 2006
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2000=100

	Jan 10th	Jan 17th*	% change on one month	% change on one year
Dollar index				
All items	148.0	150.1	+ 4.3	+20.4
Food	130.6	132.4	+ 2.8	+12.4
Industrials				
All	170.5	172.9	+ 5.9	+29.6
Nfa†	141.0	143.1	+ 6.3	+17.1
Metals	186.5	189.2	+ 5.7	+35.6
Sterling index				
All items	127.1	129.4	+ 4.3	+27.8
Euro index				
All items	113.4	115.0	+ 2.8	+30.0
Yen index				
All items	157.2	161.3	+ 3.3	+36.0
Gold				
$ per oz	541.70	558.80	+11.2	+32.1
West Texas Intermediate				
$ per barrel	63.32	66.34	+14.9	+37.3

* Provisional. † Non-food agriculturals.

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Stockmarkets

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Market indices

	Jan 18th	2005-06 high	2005-06 low	% change on one week	% change on record high	% change on Dec 31st 2004 in local currency	% change on Dec 31st 2004 in $ terms
Australia (All Ordinaries)	4,739.8	4,817.3	3,905.5	– 0.9	– 0.9	+16.9	+11.6
Austria (ATX)	3,770.3	3,830.3	2,415.0	– 0.8	– 1.2	+55.1	+38.1
Belgium (Bel 20)	3,639.0	3,691.1	2,958.8	– 0.7	– 1.2	+24.1	+10.5
Britain (FTSE 100)	5,663.7	5,740.2	4,783.6	– 1.2	–18.3	+17.6	+ 8.0
Canada (Toronto Composite)	11,554.5	11,721.0	9,006.2	– 0.6	– 0.6	+25.0	+27.7
Denmark (OMXCB)	364.7	374.2	257.8	– 0.9	– 2.5	+41.5	+25.6
France (SBF 250)	3,353.8	3,429.0	2,633.6	– 2.1	–23.6	+27.3	+13.4
(CAC 40)	4,772.1	4,890.5	3,816.1	– 2.4	–31.1	+24.9	+11.2
Germany (DAX)*	5,395.6	5,542.1	4,178.1	– 2.5	–33.1	+26.8	+12.9
Italy (S&P/MIB)	36,024.0	36,661.0	30,645.0	– 1.4	–28.1	+16.6	+ 3.8
Japan (Nikkei 225)	15,341.2	16,455.0	10,825.4	– 6.2	–60.6	+33.5	+18.7
(Topix)	1,574.7	1,685.2	1,109.2	– 5.8	–45.4	+37.0	+21.8
Netherlands (AEX)	434.2	447.9	347.0	– 2.7	–38.1	+24.7	+11.1
Spain (Madrid SE)	1,159.7	1,184.1	950.9	– 2.0	– 2.0	+20.9	+ 7.7
Sweden (Affarsvarlden Gen)	289.2	299.4	218.9	– 3.3	–27.7	+30.7	+12.7
Switzerland (Swiss Market)	7,726.5	7,835.7	5,669.6	– 0.3	– 8.1	+35.7	+20.5
United States (DJIA)	10,854.9	11,043.4	10,012.4	– 1.7	– 7.4	+ 0.7	+ 0.7
(S&P 500)	1,278.0	1,294.2	1,137.5	– 1.3	–16.3	+ 5.4	+ 5.4
(NASDAQ Comp)	2,279.6	2,331.4	1,904.2	– 2.2	–54.8	+ 4.8	+ 4.8
Europe (FTSEurofirst 300)†	1,285.3	1,311.9	1,038.6	– 1.7	–24.6	+23.4	+ 9.8
Euro area (FTSE Euro 100)†	1,088.0	1,117.1	894.4	– 2.6	–29.8	+20.8	+ 7.5
World (MSCI)‡	1,285.2	1,311.6	1,115.0	– 2.0	–11.3	+ 9.9	+ 9.9
World bond market (Citigroup)††	635.0	662.3	608.7	+ 0.1	– 4.1	– 4.7	– 4.7

*Total return index. †In euro terms. ‡Morgan Stanley Capital International index includes individual markets listed above plus eight others, in $ terms. ††Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Jan 19th 2006

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	Trade balance*, $bn latest 12 months		Current-account balance $bn latest 12 mths		The Economist poll % of GDP, forecast 2005	2006	Exchange rate trade-weighted† 2000=100 Jan 18th	year ago	Currency units per $ Jan 18th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2005‡
Australia	− 15.0	Nov	− 43.5	Q3	− 5.9	− 5.3	117.5	112.4	1.34	1.32	2.36	1.62	1.16	+ 1.0
Austria	− 1.8	Oct	− 0.1	Oct	nil	− 0.1	103.7§	104.7	0.83	0.77	1.46	–	0.72	− 2.0
Belgium	+ 14.2	Nov	+ 8.2	Sep	+ 2.2	+ 2.2	104.1§	105.6	0.83	0.77	1.46	–	0.72	nil
Britain	−116.9	Nov	− 40.6	Q3	− 2.1	− 2.2	98.2	99.4	0.57	0.53	–	0.69	0.49	− 3.1
Canada	+ 52.7	Nov	+ 19.6	Q3	+ 1.8	+ 1.6	123.7	116.4	1.17	1.23	2.07	1.42	1.02	+ 1.3
Denmark	+ 9.2	Nov	+ 8.7	Nov	+ 2.9	+ 2.8	106.0	106.4	6.17	5.71	10.9	7.46	5.35	+ 2.8
France	− 31.6	Nov	− 34.6	Nov	− 1.2	− 1.0	106.6§	108.3	0.83	0.77	1.46	–	0.72	− 3.2
Germany	+203.6	Nov	+114.0	Nov	+ 3.9	+ 3.8	104.3§	106.2	0.83	0.77	1.46	–	0.72	− 3.9
Italy	− 11.8	Nov	− 28.3	Oct	− 1.5	− 1.4	76.3§	77.5	0.83	0.77	1.46	–	0.72	− 4.3
Japan	+ 97.6	Nov	+164.7	Nov	+ 3.5	+ 3.4	83.2	90.8	115	103	203	139	–	− 6.5
Netherlands	+ 39.3	Nov	+ 44.3	Q3	+ 4.1	+ 4.2	103.6§	105.1	0.83	0.77	1.46	–	0.72	− 1.6
Spain	− 95.2	Oct	− 80.8	Sep	− 6.5	− 6.8	77.1§	77.9	0.83	0.77	1.46	–	0.72	+ 0.3
Sweden	+ 20.3	Nov	+ 24.2	Q3	+ 7.0	+ 6.7	96.4	100.4	7.71	6.93	13.6	9.33	6.69	+ 1.2
Switzerland	+ 6.6	Nov	+ 49.3	Q3	+13.3	+12.7	106.8	107.9	1.28	1.18	2.26	1.55	1.11	− 1.6
United States	−772.7	Nov	−780.6	Q3	− 6.5	− 6.6	86.3	81.5	–	–	1.76	1.21	0.87	− 3.7
Euro area	+ 41.8	Oct	− 12.0	Oct	nil	nil	116.3	118.2	0.83	0.77	1.46	–	0.72	− 2.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 11.4	Nov	+ 6.8	Nov	na	na	81.4§	82.3	0.83	0.77	1.46	–	0.72	+ 2.1
Greece	− 34.3	Oct	− 17.0	Oct	na	na	59.8§	60.4	0.83	0.77	1.46	–	0.72	− 4.5
Iceland	− 1.5	Nov	− 2.2	Q3	na	na	109.9**	96.1	61.8	62.4	109	74.7	53.6	+ 2.0
Ireland	+ 40.5	Oct	− 3.7	Q3	na	na	93.6§	96.2	0.83	0.77	1.46	–	0.72	− 0.9
Luxembourg	− 4.6	Oct	+ 3.5	Q3	na	na	104.1§	105.6	0.83	0.77	1.46	–	0.72	− 2.3
New Zealand	− 4.6	Nov	− 9.1	Q3	na	na	136.8	132.3	1.46	1.43	2.57	1.77	1.27	+ 5.3
Norway	+ 47.8	Dec	+ 43.7	Q3	na	na	107.3	107.2	6.73	6.27	11.9	8.14	5.84	+ 15.3
Portugal	− 23.3	Oct	− 16.6	Oct	na	na	93.7**	93.7	0.83	0.77	1.46	–	0.72	− 6.0

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, November average. ‡OECD estimate.
**IMF, September average.

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Government bonds

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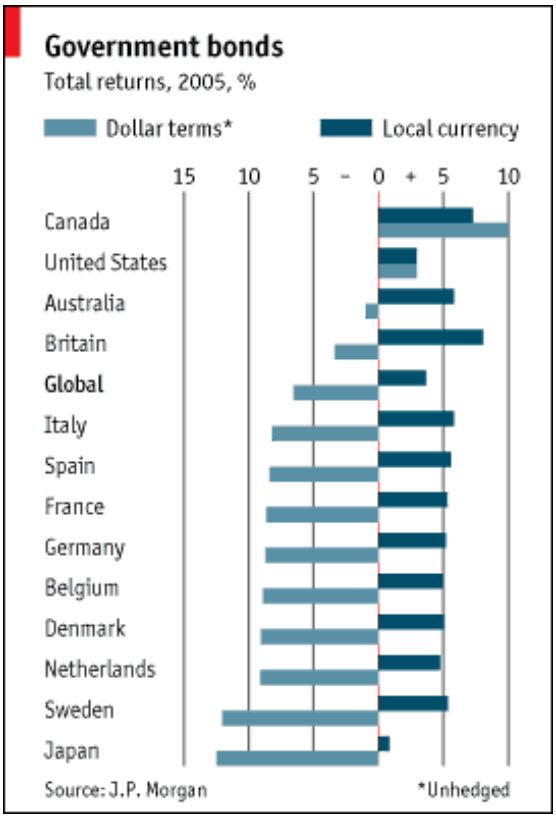

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Overview

Jan 19th 2006
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China and South Korea hold more foreign-exchange **reserves** than ever before. China's total reached $818.9 billion in December. It has added almost $50 billion-worth since the end of September. South Korea's hoard rose to $214.7 billion as of January 15th, its central bank said.

Thailand's central bank raised its benchmark interest rate to 4.25%. It has raised rates by 3.0 percentage points since August 2004 to curb inflation, running at 5.8% in the year to December.

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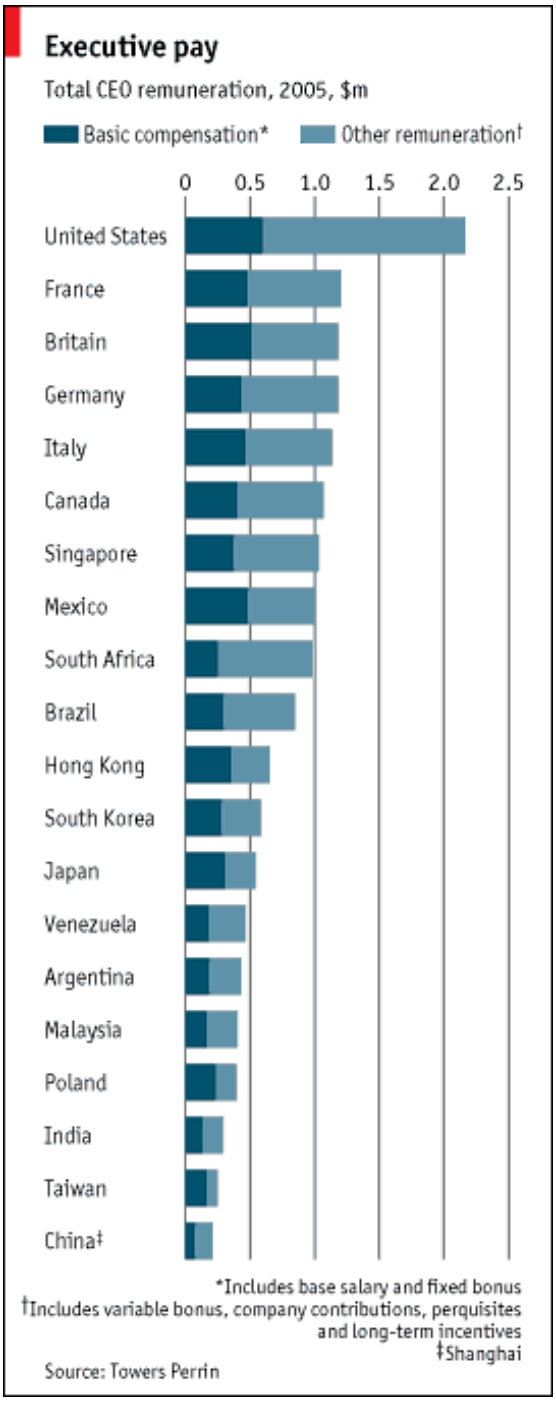
America's chief executives earn almost twice as much as their European counterparts thanks mainly to the greater use of incentive schemes, such as stock options. The typical chief executive of a $500m company in America earned $2.2m in 2005. Of this total, only $600,000, or less than 30%, came from a basic salary, according to the latest study of global executive pay by Towers Perrin, a consultancy.



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MARKETS & DATA

WEEKLY INDICATORS

Economy

Jan 19th 2006

From The Economist print edition

	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.4	Q3	+16.6	Nov	+ 1.6	Dec	+102.1	Dec	+128.5	H1	818.9	Dec
Hong Kong	+ 8.2	Q3	+ 4.1	Q3	+ 1.7	Nov	– 9.4	Nov	+21.0	Q3	124.3	Dec
India	+ 8.0	Q3	+ 6.9	Nov	+ 5.3	Nov	–37.3	Dec	–18.3	Q3	131.0	Dec
Indonesia	+ 5.3	Q3	+11.3	Nov	+17.1	Dec	+26.2	Nov	+ 0.7	Q3	31.7	Nov
Malaysia	+ 5.3	Q3	+ 6.7	Nov	+ 3.5	Dec	+25.6	Nov	+18.7	Q3	72.5	Nov
Pakistan	+ 8.4	2005†	+11.0	Jun	+ 8.5	Dec	– 8.9	Nov	– 3.7	Q3	9.6	Nov
Philippines	+ 4.1	Q3	+ 4.6	Oct	+ 6.6	Dec	– 2.2	Oct	+ 2.9	Sep	15.8	Dec
Singapore	+ 7.7	Q4	+22.4	Nov	+ 1.0	Nov	+17.3	Nov	+33.7	Q3	116.6	Dec
South Korea	+ 4.5	Q3	+12.2	Nov	+ 2.6	Dec	+23.5	Dec	+18.1	Nov	210.4	Dec
Taiwan	+ 4.4	Q3	+ 9.0	Nov	+ 2.2	Dec	+ 7.8	Dec	+ 8.9	Q3	253.3	Dec
Thailand	+ 5.3	Q3	+ 5.0	Nov	+ 5.8	Dec	– 8.0	Nov	– 3.2	Nov	49.4	Nov
Argentina	+ 9.2	Q3	+ 7.9	Dec	+12.3	Dec	+11.1	Nov	+ 4.4	Q3	25.7	Nov
Brazil	+ 1.0	Q3	+ 0.6	Nov	+ 5.7	Dec	+44.8	Dec	+14.9	Nov	64.3	Nov
Chile	+ 5.2	Q3	+ 6.2	Nov	+ 3.7	Dec	+ 9.2	Dec	– 0.2	Q3	17.0	Dec
Colombia	+ 5.8	Q3	+ 0.5	Oct	+ 4.9	Dec	+ 1.5	Oct	– 1.7	Q3	14.8	Dec
Mexico	+ 3.3	Q3	+ 3.0	Nov	+ 3.3	Dec	– 8.6	Nov	– 8.4	Q3	72.7	Nov
Peru	+ 7.9	Nov	+ 7.6	Nov	+ 1.5	Dec	+ 4.6	Nov	+ 0.8	Q3	13.2	Dec
Venezuela	+ 9.8	Q3	+10.8	Oct	+14.4	Dec	+28.2	Q3	+21.6	Q3	24.4	Oct
Egypt	+ 5.2	Q1	+ 4.0	2005†	+ 3.4	Nov	–11.3	Q3	+ 1.8	Q3	20.9	Dec
Israel	+ 5.7	Q3	–15.2	Oct	+ 2.4	Dec	– 7.9	Dec	+ 2.4	Q3	27.9	Dec
Saudi Arabia	+ 6.2	2005‡	na		+ 1.0	Sep	+84.6	2004	+51.9	2004	27.6	Nov
South Africa	+ 4.9	Q3	+ 3.7	Nov	+ 3.4	Nov	– 3.4	Nov	–10.3	Q3	18.6	Dec
Czech Republic	+ 4.9	Q3	+ 7.2	Nov	+ 2.2	Dec	+ 1.5	Nov	– 3.4	Q3	29.3	Dec
Hungary	+ 4.5	Q3	+ 7.7	Nov	+ 3.3	Dec	– 3.5	Nov	– 8.7	Q3	17.5	Dec
Poland	+ 3.7	Q3	+ 8.5	Nov	+ 0.7	Dec	– 3.1	Nov	– 4.9	Nov	39.8	Dec
Russia	+ 7.0	Q3	+ 5.5	Nov	+10.9	Dec	+117.6	Nov	+81.2	Q3	175.9	Dec
Turkey	+ 7.0	Q3	+10.7	Nov	+ 7.7	Dec	–43.2	Nov	–21.7	Nov	47.9	Nov
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+10.8	Q3	+10.4	Nov	+ 3.6	Dec	– 2.5	Oct	– 1.4	Nov	1.8	Nov
Latvia	+11.4	Q3	+ 5.9	Nov	+ 7.0	Dec	– 2.9	Nov	– 1.9	Nov	2.2	Nov
Lithuania	+ 7.6	Q3	na		+ 3.0	Dec	– 3.6	Nov	– 1.7	Nov	3.5	Nov
Slovakia	+ 6.2	Q3	+ 5.7	Nov	+ 3.7	Dec	– 1.9	Nov	– 2.8	Sep	14.9	Nov
Slovenia	+ 3.7	Q3	+ 7.3	Nov	+ 2.3	Dec	– 1.6	Nov	+ 0.1	Nov	8.0	Oct

*Excluding gold, except Singapore; IMF definition. †Year ending June. ‡Economist Intelligence Unit estimate.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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MARKETS & DATA

WEEKLY INDICATORS

Financial markets

Jan 19th 2006

From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Jan 18th		Dec 31st 2004	
	Jan 18th	year ago	Jan 18th	% a year		one week	in local currency	in $ terms
China	8.07	8.28	14.2	2.05	1,294.5	+1.8	– 2.7	– 0.2
Hong Kong	7.75	7.80	13.7	3.98	15,481.2	-1.1	+ 8.8	+ 9.1
India	44.3	43.7	78.1	6.17	9,237.5	-2.2	+ 39.9	+ 37.3
Indonesia	9,500	9,285	16,746	14.13	1,193.2	-5.4	+ 19.3	+ 16.6
Malaysia	3.76	3.80	6.62	3.26	901.3	-0.9	– 0.7	+ 0.5
Pakistan	59.9	59.4	105.54	9.01	10,235.2	+2.5	+ 64.6	+ 63.2
Philippines	52.8	54.8	93.0	7.38	2,125.5	-1.2	+ 16.6	+ 24.0
Singapore	1.63	1.63	2.87	3.31	2,359.3	-2.5	+ 14.2	+ 14.4
South Korea	992	1,008	1,749	4.16	1,352.9	-3.0	+ 51.0	+ 57.6
Taiwan	32.1	30.8	56.6	1.65	6,498.9	-3.5	+ 5.9	+ 4.4
Thailand	39.4	38.4	69.5	4.50	736.4	-3.6	+ 10.2	+ 8.6
Argentina	3.05	2.95	5.37	9.38	1,645.5	-0.3	+ 19.6	+ 16.7
Brazil	2.32	2.63	4.09	17.95	35,805.0	-0.4	+ 36.7	+ 56.5
Chile	535	588	944	5.16	9,328.1	-1.4	+ 4.1	+ 8.0
Colombia	2,272	2,329	4,005	6.20	10,650.9	+6.6	+145.1	+153.7
Mexico	10.6	11.1	18.6	7.89	18,266.0	-4.7	+ 41.4	+ 49.2
Peru	3.38	3.26	5.96	3.57	4,904.3	+4.9	+ 32.2	+ 28.2
Venezuela	2,585§	2,667§	4,557	11.63	24,333.0	+10.8	– 18.8	– 19.0
Egypt	5.74	5.81	10.11	8.54	62,185.7	+4.9	+152.9	+167.7
Israel	4.63	4.33	8.16	4.91	846.9	+1.1	+ 31.5	+ 22.8
Saudi Arabia	3.75	3.75	6.61	5.13	17,635.3	-0.2	+114.9	+114.9
South Africa	6.06	5.91	10.7	7.10	18,304.1	-1.6	+ 44.6	+ 34.4
Czech Republic	23.8	22.6	42.0	2.13	1,498.4	-1.2	+ 45.2	+ 36.1
Hungary	208	185	367	6.10	22,119.5	-1.4	+ 50.0	+ 30.2
Poland	3.19	2.99	5.62	4.49	37,854.9	-0.6	+ 42.1	+ 33.5
Russia	28.3	27.7	49.8	12.00	1,235.0‡	+1.5	+105.0	+101.1
Turkey	1.34	1.28	2.35	14.80	42,622.9	+1.7	+ 70.7	+ 72.3
EM (MSCI)*	1.00	1.00	1.76	na	738.7	-1.9	+ 36.2	+ 36.2
EMBI+†	1.00	1.00	1.76	na	372.6	+0.4	+ 13.1	+ 13.1

*Emerging Mkts. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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